

**PROPOSED FISCAL YEAR 2008  
BUDGET REQUEST FOR THE  
DEPARTMENT OF INTERIOR'S  
OFFICE OF INSULAR AFFAIRS**

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**OVERSIGHT HEARING**

BEFORE THE  
SUBCOMMITTEE ON INSULAR AFFAIRS  
OF THE  
COMMITTEE ON NATURAL RESOURCES  
U.S. HOUSE OF REPRESENTATIVES  
ONE HUNDRED TENTH CONGRESS

FIRST SESSION

February 27, 2007

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**OVERSIGHT HEARING ON THE “PROPOSED  
FISCAL YEAR 2008 BUDGET REQUEST FOR  
THE DEPARTMENT OF INTERIOR’S OFFICE  
OF INSULAR AFFAIRS”**

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**February 27, 2007  
U.S. House of Representatives  
Subcommittee on Insular Affairs  
Committee on Natural Resources  
Washington, D.C.**

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The Subcommittee met, pursuant to call, at 10:03 a.m., in Room 1324, Longworth House Office Building, Hon. Donna Christensen [Chairwoman of the Subcommittee] presiding.

Present: Representatives Christensen, Bordallo and Fortuño.

**STATEMENT OF THE HONORABLE DONNA M. CHRISTENSEN,  
A DELEGATE IN CONGRESS FROM THE VIRGIN ISLANDS**

Mrs. CHRISTENSEN. Good morning. The oversight hearing by the Subcommittee on Insular Affairs will come to order. The Subcommittee is meeting today to hear testimony on the proposed Fiscal Year 2008 budget request from the Department of Interior’s Office of Insular Affairs. Under Committee Rule 4(g), the Chairman and Ranking Member usually are the only ones to make opening statements, but today we will depart from that, without objection, and allow every member on the Subcommittee to make an opening statement if they so wish.

But I am very pleased and honored to call this first meeting of the Subcommittee on Insular Affairs of the 110th Congress to order. I am looking forward to an active and productive Subcommittee, and I want to thank Chairman Rahall for reinstating the Subcommittee and giving me the opportunity to chair it. I also want to welcome my colleague, Congressman Fortuño, and welcome the insights and leadership that he is going to bring to our deliberations. And, of course, on this first meeting, I want to welcome all the members of the Subcommittee.

It is a very special honor and pleasure also to welcome our friends and the leaders of our territories, the Governors. The two who are here are from the far-off Pacific insular areas, and we thank them for being here with us today.

When the Committee was first under the Chairmanship of my predecessor and former Virgin Islands Congressman Ron DeLugo, we took advantage of the Governors being in Washington for the

annual National Governors Association meeting to invite them to come before the Subcommittee, your home here in Congress, to comment on the proposed budget of the Office of Insular Affairs as well as to inform us of any issues facing you at home that the Federal Government could be helpful with. So I want to welcome The Honorable Felix Camacho, the Governor of Guam, and The Honorable Togiola Tulafono, the Governor of American Samoa. Unfortunately The Honorable Benigno Fitial, the Governor of the Commonwealth of the Northern Mariana Islands, was unable to travel to Washington for the annual meeting this year because of pressing business at home, including a visit by the senior staff of the Senate committee to the CNMI. I also regret that as of now, my own Governor, The Honorable John deJongh, Jr., is unable to be here today, but both have submitted statements for the record.

Mrs. CHRISTENSEN. And soon we look forward to welcoming the Deputy Assistant Secretary David Cohen, who I understand is just getting off a plane.

As we are keenly aware, the Office of Insular Affairs has broad general authority to provide for the special needs and concerns of the U.S. insular areas. President Bush in his Fiscal Year 2008 budget has proposed sending \$403.8 million for the Office of Insular Affairs of which \$79.8 million is in current appropriations. That figure is \$425,000 below the 2007 continuing resolution, but \$560,000 above the President's Fiscal Year 2007 budget request. \$324.1 million of the Fiscal Year 2008 figure includes \$119 million in estimated income tax payments to Guam and the Virgin Islands, and \$205.1 million in payments under the Compacts of Free Association. Programs funded under the 2008 fiscal year budget request will continue long-term efforts throughout the territories and freely associated states. Over \$200 million in Compact of Free Association Sector Grants will be included in the 2008 budget. More than \$12 million will be requested for a variety of technical assistance programs, including ongoing efforts on the brown tree snake control, insular management controls, coral reef conservation, maintenance assistance and water and wastewater projects.

Some questions we hope to receive answers from the Office of Insular Affairs include the specifics of the competitive allocation system for the Covenant Improvement Project Grants and whether more consideration should be given to those projects that are under court orders, and what are their plans for addressing the potential catastrophes looming for the economies of American Samoa and the CNMI and, to a lesser extent, my home islands as we continue to stave off attempts by the Treasury Department to effectively neuter the successful economic development program that Congress put in place to assist with our economic development. In my opinion, it is one that could and should serve as a model to our sister territories, which are all in need of an economic shot in the arm.

The budget of the Office of Insular Affairs has either remained constant or been reduced over the last 5 fiscal years, from a high of \$102 million in 2002 to the proposed \$79.7 million for 2007. All the while the needs and the challenges facing the islands have increased.

We have also recently heard testimony at the committee on the severe fiscal challenges that are not being adequately met, and we

heard those from the Office of Inspector General and from the Government Accountability Office.

It is my hope that as Chair of this Subcommittee, and with the assistance of my colleagues, that we will explore today whether adequate resources are being given to the OIA to enable them to address the unique, important challenges that are faced by these, our most vulnerable members of the American family, the members of the insular areas. In this regard, I look forward to hearing from our witnesses, and now I yield to my friend, the Ranking Member on the Subcommittee, The Honorable Luis Fortuño, for any opening statements he wishes to make.

[The prepared statement of Mrs. Christensen follows:]

**Statement of The Honorable Donna M. Christensen,  
Chairwoman, Subcommittee on Insular Affairs**

I am pleased and honored to call the first meeting of the Subcommittee on Insular Affairs for the 110th Congress to order.

I am looking forward to an active and productive subcommittee and I want to thank Chairman Rahall for re-instating the subcommittee and giving me the opportunity to chair it. I also want to welcome my colleague, Congressman Fortuño, and the insights and leadership he will bring to our deliberations and on this first meeting to welcome all of the members of the subcommittee.

It is a special pleasure to welcome our friends, the governors from the far off pacific Insular Areas and thank them for being here with us today.

When this subcommittee was under the Chairmanship of my predecessor and former Virgin Islands Congressman, Ron de Lugo, we took advantage of the governors being in Washington for the annual National Governor's Association meeting to invite you to come before the subcommittee—your home here in the Congress—to comment on the proposed budget of the Office of Insular Affairs as well as to inform us of any issues you are facing at home that the federal government could be helpful with.

And so, I want to welcome The Honorable Felix Camacho, the Governor of Guam and The Honorable Togiola Tulafono, the Governor of American Samoa. The Honorable Benigno R. Fitial, the Governor of the Commonwealth of the Northern Mariana Islands was unable to travel to Washington for the annual meeting this year because of pressing business at home including a visit by the senior staff of the Senate committee to the CNMI. I regret that my own Governor, The Honorable John P. deJongh, Jr. is unable to be here today. Both have submitted statements for the record.

Of course we also welcome Deputy Assistant Secretary, David Cohen as well.

As we all are keenly aware, the Office of Insular Affairs has broad general authority to provide for the special needs and concerns of the U.S. Insular Areas. President Bush, in his Fiscal Year 2008 budget, has proposed spending \$403.8 million for the Office of Insular Affairs (OIA), of which \$79.8 million is in current appropriations.

This figure is \$425,000 below the 2007 Continuing Resolution and \$560,000 above the President's FY 2007 budget request. \$324.1 million of the FY08 figure includes \$119 million in estimated income tax payments to Guam and Virgin Islands and \$205.1 million in payments under the Compacts of Free Association.

Programs funded under the FY 2008 Budget Request will continue long-term efforts throughout the territories and Freely Associated States. Over \$200.0 million in Compact of Free Association Sector Grants will be included in the 2008 budget. More than \$12.0 million will be requested for a variety of Technical Assistance programs, including ongoing efforts on Brown Tree Snake control, insular management controls, coral reef conservation, maintenance assistance, and water and wastewater projects.

Some questions we hope to receive answers from the Office of Insular Affairs include the specifics of the competitive allocation system for the Covenant Improvement Project (CIP) grants and whether more consideration should be given to those projects that are under court orders; and what are their plans for addressing the potential catastrophes looming for the economies of American Samoa and the CNMI and to a lesser extent my home islands as we continue to stave off attempts by the Treasury Department to effectively neuter the successful economic development program that Congress put in place to assist with our economic development. In my

opinion it is one that could and should serve as a model for our sister territories which are all in need of an economic shot in the arm.

The budget of the Office of Insular Affairs has either remained constant or been reduced over the last five fiscal years—from a high of \$102 million in FY 02 to the proposed \$79.7 million for FY07—all the while the needs and challenges facing the islands have increased. We have also recently heard testimony at the Committee on the severe fiscal challenges that are not being adequately met from the office of the Interior Inspector General and the GAO.

It is my hope, as chair of this subcommittee and with the assistance of my colleagues, to explore whether adequate resources are being given to OIA to enable them to address the unique, important challenges that are faced by these our most vulnerable members of our American family; the residents of the Insular Areas. In this regard, I look forward to hearing from our witnesses.

I now yield to my friend, the Ranking Member on the Subcommittee, The Honorable Luis Fortuño for any opening statement he wishes to make.

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**STATEMENT OF THE HONORABLE LUIS FORTUÑO, THE  
RESIDENT COMMISSIONER IN CONGRESS FROM PUERTO RICO**

Mr. FORTUÑO. Thank you very much, Madam Chairwoman. First of all, I want to congratulate you on being selected to chair this Subcommittee. I am truly enthusiastic about this honor being bestowed upon my friend from the U.S. Virgin Islands.

It is appropriate that our first hearing together involves the review of the President's Fiscal Year 2008 budget request, which reflects the budget priorities of the Department of Interior's Office of Insular Affairs. While this priority may not always match yours or even mine sometimes, I welcome this historic time for a Delegate and a Resident Commissioner to receive policy on the insular areas, and for a chance for us to work together with the President and the Secretary of Interior to work forward in a productive fashion for the benefit of all the people affected by at least the decision of the Subcommittee.

I join you in welcoming our witnesses today, The Honorable Togiola Tulafono, the Governor of American Samoa; The Honorable Felix Camacho from Guam; and Deputy Assistant Secretary David Cohen.

Madam Chairwoman, the President's budget proposals have balanced the increase in funding for the Office of Insular Affairs to \$403.8 million, an increase of \$2 million over the present Fiscal Year 2007 continuing resolution. What I recognize, we are all living within difficult budget restraints. I look forward to hearing from the Governors here today about the needs and priorities of their communities as well as from the administration witness as to how the Office of Insular Affairs can best administer these scarce budget resources more efficiently for the benefit of all the insular areas.

Thank you again, Madam Chairwoman. I look forward to working with you on these issues over the course of this Congress. I yield back.

Mrs. CHRISTENSEN. Thank you.

[The prepared statement of Mr. Fortuño follows:]

**Statement of The Honorable Luis Fortuño, Ranking Republican Member,  
Subcommittee on Insular Affairs**

Madam Chairwoman, I want to congratulate you on being selected to Chair this Subcommittee. It is appropriate that our first hearing together involves a review of



the President's Fiscal Year 2008 Budget Request which reflects the budget priorities of the Department of Interior's Office of Insular Affairs.

While these priorities may not always match yours, or even mine sometimes, I welcome this historic time for a Delegate and Resident Commissioner to oversee policy on the Insular Areas and a chance for us to work together with the President and the Secretary of Interior to move forward in a productive fashion for the benefit of all the people affected by the legislation of this Subcommittee.

I join you in welcoming our witnesses today: The Honorable Togiola T.A. Tulafono, Governor of American Samoa; The Honorable Felix Camacho from Guam; and from the Administration, Deputy Assistant Secretary David Cohen (or Nik Pula) of the Interior Department's Office of Insular Affairs.

Madam Chairwoman, the President's budget proposes a modest increase in the funding for the Office of Insular Affairs to \$403.8 million, an increase of \$2.0 million over the present Fiscal Year 2007 continuing resolution.

While I recognize we are all living within difficult budget restraints, I look forward to hearing from the Governors here today about the needs and priorities of their communities, as well as from the Administration witness, as to how the Office of Insular Affairs can best administer these scarce budget resources most efficiently for the benefit of all the Insular areas.

Thank you Madame Chairwoman. I look forward to working with you on these issues over the course of this Congress.

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Mrs. CHRISTENSEN. The Chair now recognizes The Honorable Congresswoman from Guam Madeleine Bordallo for an opening statement.

**STATEMENT OF THE HONORABLE MADELEINE BORDALLO,  
A DELEGATE IN CONGRESS FROM GUAM**

Ms. BORDALLO. Thank you. Thank you for calling this hearing today, Chairwoman Christensen. To me this is a very important moment as we have the first oversight hearing of the newly reestablished Subcommittee on Insular Affairs. And I am very thankful to you, Chairwoman Christensen, to Chairman Rahall and to Congressman Faleomavaega for reestablishing this Subcommittee to bring greater focus on the programs administered by the Office of Insular Affairs and on Federal policy affecting the territories.

This hearing on the President's proposed budget for the Office of Insular Affairs provides to us an opportunity to hear from the Governors of the territories. I want to welcome all of you who have traveled great distances to be here with us today, and a very warm hafa adai to Guam's Governor, The Honorable Felix P. Camacho. Talofa to the Governor of the American Samoa, Governor Tulafono.

Each of our territories are facing economic challenges, and I am interested to hear how the Office of Insular Affairs is helping the territories to cope with these challenges. In particular, while Guam's economic forecast is bright due to the Pentagon's intention to relocate a number of Armed Forces to Guam, the military build-up presents serious challenges to our local government. I hope to hear from Governor Camacho today on what some of these challenges are and how best the Department of Interior can assist the Government of Guam in the years ahead.

Finally, let me make one comment on the Office of Insular Affairs Capital Improvement Grant Program for the territories. We are not talking about a large amount of money here. Annual allocations for the territories from this program amount to \$27.72 million. For this reason I believe that it is important that a very clear set of priorities and transparent process be established for allocating these funds.

I would like to have a better understanding from the Deputy Assistant Secretary of the evaluation process that has been developed regarding the financial management of the individual governments that affects the annual allocation received under this program.

I would also like to hear your comments, Mr. Cohen—he is not here yet—regarding Congress's intent that Federally mandated court-ordered projects be given a higher priority than other projects as noted in the colloquy during House floor debate on the Fiscal Year 2005 Interior Appropriations Act and the committee's accompanied report that year.

Again, let me welcome all of you, and let me extend my thanks to Chairwoman Christensen. Thank you.

Mrs. CHRISTENSEN. Thank you for your opening statement.

Mrs. CHRISTENSEN. The Honorable Eni Faleomavaega is on his way also from the airport, and we will give him an opportunity to make an opening statement when he arrives.

At this time we will be pleased to turn to the panel, and we will begin with the testimony from the Governor of American Samoa, The Honorable Governor Tulafono.

**STATEMENT OF TOGIOLA T.A. TULAFONO,  
GOVERNOR, AMERICAN SAMOA**

Governor TOGIOLA. Thank you very much, Madam Chairlady. Talofa and good morning to all the members of the Subcommittee.

At the outset, let me just say, Madam Chairlady, that I am very grateful for the opportunity to reopen this dialogue through the recreation of this Subcommittee and allowing the Governors of the insular areas to be able to participate in the budget process. It has been a long time since an elected Governor of American Samoa was able to speak directly to Members of Congress about the budget process and what we are doing.

I want to congratulate you on your ascent to the Chairmanship of the Subcommittee and all the insular area members in this committee. We want to register also our gratitude and appreciation to the Chairman of the Subcommittee on Resources for recreating and reinstatement of this Subcommittee.

We have submitted a written statement, Madam Chairlady, and I am now going to try and rehash the matters we have stated. I am going to digress a little bit in our oral statement to supplement our submission today. I suppose the basic question here is how do we feel about the funding and the mechanism in which it is done for the insular areas and especially for American Samoa.

Madam Chair and the honorable Members, you all know that no matter who is doing the talking, there will always be more needs and wants, and there will always be insufficient funds to meet all those needs. For our part today, let me just say, American Samoa appreciates the fiscal restraints of our national government, and we appreciate the fact that we are getting help from the Federal Government for our operation. Of course, these funds are nowhere near what American Samoa needs, and, of course, we can spend all day going through all the things we need to develop and sustain the economy and the quality of life for the people of American Samoa, but if you approve what has been proposed, I assure you they will be put to the best use we have planned.

I would venture to say today that it is my hope that we will convince the United States Department of Interior that we need to revisit our budget system and come up with a plan that will adequately anticipate the needs and unique circumstances of American Samoa and reflect that in our submissions to Congress for approval.

Two things I would like to point out. The budget system that we are using today to address our operations and developments in American Samoa as a U.S. territory is the same system that has been there for many, many years, and that has never changed. Very little has changed. Two, the same development plan that is being utilized for planning the progress of American Samoa is the same that it has been for the last 40 years.

It is my hope that sometime soon, and through the process of the newly reinstated Subcommittee, that we will be able to forge Federal policy for American Samoa that will transcend shifts in policies and changes in attitude of our national government that are made to accommodate the global policies of our Nation, and leaving insular areas struggling to find a way to fit in the mix. American Samoa and the insular areas are so vulnerable to these policy changes and shifts that today any development efforts in our part is completely stagnant by the fact that we have lost the benefits of section 936, headnote 3A and the uncertainty of the minimum wage policies that are to be applied to us.

We are not afraid of being self-sufficient and self-sustained, but like any other State or territory, we need to have the ability to build our economy to be self-sufficient and self-sustaining. Unfortunately we are extremely limited in our ability to do so without a consistent, well-considered plan that will keep us competitive in our development efforts like any other State or country. That requires a consistent and sustainable Federal policy.

The last time there was a well-considered and well-supported plan for American Samoa, I hate to say, was in the early 1960s, but that, too, was in response to an article which called American Samoa the shame of the U.S. in the Pacific. Only at that time there was a consistent policy that would build infrastructure, put in new hospitals, new schools, a new airport, and created a new corporation for developmental efforts.

We certainly do not want to wait until another article like that, nor do we want to go back to those times, but we cannot do it alone, and we are looking to your leadership and your guidance to help us develop these kinds of policies for at least—for our part, American Samoa.

In terms of our economic development efforts, we are indeed doing all we can with the resources we have together with the resources allotted to us in order to build a sustainable economy that will sustain American Samoa and give our people a quality of life just like any other American.

The operation grant that we receive through the Department of Interior is divided in five pieces: One, to support the operation of the high court that is still under the control of the Department of Interior. Two, of the remaining portion of those funds, I ask Interior to split that in four ways between our community college, Department of Education and our medical center. I did ask Interior

to set aside \$2 million of that to secure the consistent supply of medicine and drugs for our medical center. That was accomplished through the efforts of Congressman Faleomavaega in earmarking that grant and setting aside the \$2 million, and we are grateful.

For the funds allocated for capital improvements, the government submits to DOI a 5-year plan requesting funding based on the recommended priorities we provide in a 5-year plan. DOI submits this funding to Congress for approval. When approved, we follow the priorities we provided in the plan for CIPs. Occasionally we require some reprogramming, and we have received the cooperation of DOI in making sure that our needs are met through that program.

Beginning with this fiscal year, I have prioritized the development of fiberoptic submarine cable over the next 5 years. While our satellite communication capability is great, it has been proven—it has proven that it will not support our development efforts. The fiberoptic cable will allow us to expand those development efforts and truly achieve diversification, which is something that has been talked about in American Samoa since 1950 and has never been possible.

Even with the availability of Federal incentives as section 936, headnote 3A and lower wages than in the United States, only two U.S. companies ever relocated their plants into American Samoa. Since then every Governor that came to American Samoa talked about diversification and never was able to accomplish anything close to it. Madam Chairlady, the fiberoptic promises to bring about that diversification for American Samoa. Perhaps it is a timely project because the future of our counties are really very uncertain. The cable is already inspiring businesses as call centers, banking institutions, educational institutions to inquire as to when it may be available.

I would like to register our gratitude and appreciation to Mr. Cohen and the Office of Insular Affairs for their support of this endeavor. I would also like to acknowledge our appreciation for the business development conferences that the Department of Interior has sponsored for the last few years to help us identify and come together with businesses that may be interested in investing in American Samoa. I will say through those conferences we have been able to meet with people interested in fiberoptic development, and we are moving forward with that project. And I realize that the Department of Interior has set aside \$3 million every year for the next 4 years in that submission to help us accomplish that purpose, and we will ask for your support of that project.

I will stop there and will answer any questions you may have. Mrs. CHRISTENSEN. Thank you.

[The prepared statement of Governor Togiola<sup>1</sup> follows:]

**Statement of The Honorable Togiola T.A. Tulafono,  
Governor of American Samoa**

Talofa. Honorable Chairman and distinguished members of this Committee; it is with great pleasure and honor that I appear here today at your invitation to give

<sup>1</sup>According to traditional Samoan cultural protocol, Governor Togiola T.A. Tulafono is addressed by his matai title of "Togiola" and is referred to as "Governor Togiola." However, those not familiar with Samoan culture address him as "Governor Tulafono." Both forms of address are correct.

testimony on the Fiscal Year 2008 budget of the Office of Insular Affairs. I thank you for this opportunity to convey to you the importance of this funding for the territory of American Samoa, our operations and our economic development. I also want to greet and thank all of the Committee's new members as well.

### **Introduction**

American Samoa, located in the Central South Pacific is the only United States territory south of the equator. The islands of eastern Samoa became part of the U.S. in 1900 and 1904. A central premise of ceding eastern Samoa to the U.S. was to preserve the rights and property of the islands' indigenous inhabitants. American Samoa's constitution requires the government to protect persons of Samoan ancestry from the alienation of their lands, protect against the destruction of the Samoan way of life and language, and to encourage business enterprise among persons of Samoan ancestry. American Samoa, in turn, ceded authority over its lands and pledged its allegiance to the United States of America. The depth of our commitment is evident today in the disproportionately high share and the contributions of our people in the U.S. military, especially their dedicated service in past and current wars.

### **Economic Development Conditions in American Samoa:**

American Samoa has made extraordinary progress in recent decades, considering it only began its own pursuit of modern development since the Second World War. This is a relatively brief period from a development standpoint. In addition to building modern economic, education, health care and infrastructure systems, American Samoa has essentially become self-governing under the general authority of the U.S. Executive Office (DOI). However, we have a very long way to go. For example, our per capita income is only about one-fifth the U.S. average, and poverty levels in American Samoa are almost six times the national average. American Samoa also suffers from high rates of substandard housing and our public services and facilities remain well below U.S. standards.

At the same time, American Samoa is subject to the same forces that affect economies, large and small, throughout the world. Rising world trade and globalization, as we often refer to it, is changing our economies dramatically as industries seek lower and lower cost venues. American Samoa, however, does not have the options that are available to major industrial economies. Our productivity, i.e. output per worker, is only about one-fifth that of the U.S. average. In addition we have the added issues of distance to markets and sources of supply and the diseconomies of relatively small size which affects our labor force quantity and skill characteristics. We do not have the development options that are available to most of the US.

On the other hand, we are not really a developing economy either (or less developed, if you prefer) in the sense that these terms are used to describe nations in or bordering on abject poverty. Because of our relationship with the U.S. we have had access to special advantages. We have received financial support, federal corporate tax credits, and duty free access to U.S. markets and a special procedure for establishing minimum wages. We have had the flexibility to operate our own customs and immigration. These benefits have helped us rise above the economic fate that has befallen island nations similarly endowed and situated throughout the world.

These advantages were largely responsible for our ability to retain our tuna cannery industry for fifty years. Furthermore, the loss of these benefits threatens to cause our cannery industry to seek lower cost locations elsewhere. Much of our success to date has been based upon these benefits which are now rapidly disappearing or threatened. There is nothing on the horizon or in the offing to replace these benefits.

The departure of the canneries from American Samoa would wipe out one-half of the total jobs in American Samoa directly and indirectly. This would be a catastrophe for any economy, but it would be worse for a small isolated area like American Samoa.

Furthermore, there could be very serious additional contingency costs for the Federal Government if the canneries were to leave American Samoa. The Federal Government would likely be petitioned for assistance to deal with very serious and protracted problems including unemployment, retraining, relocation assistance, business failures, plummeting local revenues for essential public services and other needs that could emerge in such an economic disaster.

Unfortunately, the threat to American Samoa's economy does not end with the revocation of corporate tax credits and the diminishing value of our duty free access to the U.S. because of declining tariffs worldwide. There are pressures now to equalize U.S. and American Samoa minimum wage rates. There is even talk of bringing

American Samoa under U.S. Immigration, possibly even under U.S. Customs. These are the characteristics that have helped us to succeed in economic development. If we lose these special conditions, American Samoa could face insurmountable economic development barriers in the future.

However, the U.S. Congress has taken notice of our plight and we are hopeful that help is on the way. Last year in connection with the extension of our cannery tax credit, the Congress provided in its report:

“The two-year credit allowed by the provision is intended to provide additional time for the development of a comprehensive, long-term economic policy toward American Samoa. It is expected that in developing a long-term policy, non-tax policy alternatives should be carefully considered. It is expected that long-term policy toward the possessions should take into account the unique circumstances in each possession.”

I am concerned that we don't know enough about what Congress wants except for the few words in the Committee/staff report on the tax bill I just cited. We are hopeful that this opportunity is taken to examine the critical ways in which federal legislation and policy affect American Samoa's development including tax credits, the minimum wage, immigration and customs, and a variety of other areas.

I hope that the American Samoa Government, American Samoa's Congressional Representative, and the Office of Insular Affairs will be part of the design and conduct of the preparation of a long-term economic development policy for American Samoa.

#### **ASG Economic Development Programs:**

For our part, we are working with you and the Department of Interior on tax credit alternatives. We are also moving ahead on the cannery impact analysis which will nail down cannery reduction impacts, remedial programs and redevelopment alternatives. Additionally, in conjunction with the Office of Insular Affairs, my administration has submitted to our Representative, for his review, consideration and possible adoption, a proposal for a tax incentive package that we believe focuses on promoting business investment within American Samoa. With the honorable Congressman's help and the help of this Committee, a tax incentive package would attract new businesses and help us overcome our disadvantages in distance, scarcity of transportation and reliance on federal grants to fund basic services.

In addition to promoting federal tax incentives for businesses willing to invest in American Samoa, ASG is pursuing a number of complementary initiatives such as streamlining the business permitting and licensing process in order to make the investment climate more business friendly. Through technical assistance funding from the Office of Insular Affairs, ASG will make the process of attaining a business license much simpler through electronic means. Additionally, the ASG will do away with the inefficient waiting periods in order for multiple agencies to sign off on permits by consolidating hearings and allowing for a “one-window” approach to electronically apply for licenses and permits through the internet and to electronically attach and store licensing and permitting documentation. Approval of licenses and permits will take place electronically, without sacrificing the safeguards that any one agency provides.

ASG is also pursuing a number of new programs which will encourage investment in the territory, including the establishment and administration of the territory's Low Income Housing Tax Credit Program, which has the potential to infuse eighteen million grant-like dollars into the local economy and help foster our private construction sector. And this is in addition to the provision of housing for our low-income population. Through technical assistance funding, we hope to bring this program into reality within the next two years.

These are only a few of the programs that ASG is able to pursue through the technical assistance funding available through the Office of Insular Affairs. This program is invaluable to our development as a territory, and I express my wholehearted support for its continuation and expansion into the future.

#### **Diversified Industries**

American Samoa has had some success over the years in attracting diversified manufacturing. Today, a key industry targeted for development is technology based (e-Commerce) which depends on skilled workers and well-developed internet-based communication systems.

We recognize and thank the Department of Interior, Office of Insular Affairs, for its foresight in requesting funding for our undersea fiber-optic cable. In recent times, American Samoa has entertained proposals from U.S. companies looking to do business in the territory. The types of business contemplated by these companies require broadband Internet capability that only a hard landline connection may

provide. American Samoa has made it clear to the Office of Insular Affairs that we are prepared to follow the recommendations of past economic advisory councils and commissions, and pursue aggressively, any and all opportunities to cultivate e-commerce and export of services via information technology from American Samoa.

Among other economic development projects and proposals that are currently being pursued are a local fish processing facility, co-ops for local fishermen and farmers, and numerous niche markets within the Tourism industry.

#### **Operational Grants**

ASG receives direct operating grants from DOI of \$22 million per year. I can assure this Committee that these operational grants are absolutely vital to the well being of our people. ASG's only full-scale health care institution, the LBJ Tropical Medical Center, and the Department of Education are the major recipients of the operational grant funds.

The operations grants have not had a significant increase for over 2 decades. During that time, the population has doubled, and the cost of living has increased approximately sixty percent. American Samoa has struggled to maintain essential government services, but this can hardly be done given the state of the economy in American Samoa.

#### **Operations Maintenance Improvement Program (OMIP)**

One of the biggest challenges that ASG deals with on a regular basis, especially given the corrosive nature of a tropical environment, is maintenance and improvement of facilities. Through the OMIP program, ASG is able to access funds that would otherwise have to come from other portions of the ASG budget. Currently, our own community college, ASCC, is availing itself of the opportunity to set up its own maintenance program utilizing software that is currently being used in other insular areas.

#### **Capital Improvement Projects**

Currently, American Samoa receives \$10.5 million in CIP funding. This funding is directly responsible for developing critical infrastructure in the territory. From the construction of schools and hospital facilities, to the hardening of utilities which aid in recovery following disasters, this funding is essential for developing the territory's infrastructure and making the territory more attractive for development. Again, it is my recommendation that this specific program be continued at its current level, and if possible, expanded to increase the funding of additional necessary infrastructure in the islands.

#### **Island Fellows Program**

Agencies of the American Samoa Government have benefitted directly from the Office of Insular Affairs' Island Fellows Program. One agency in particular, the Development Bank of American Samoa, is especially satisfied with this program. Over the past year, the Development Bank has increased the number of programs it administers. The Bank encourages the continuation of this program which promotes forward-thinking analysis by innovative young scholars as an aid to economic development.

#### **Special Industry Committees**

Of particular interest in recent months is the special industry committee process by which American Samoa's minimum wages are set. As I have stated in the past, it is the position of my administration that these special industry committees work for our territory. They are responsive and they take into account the unique factors presented by American Samoa's fledgling economy. Unless and until a more responsive and effective approach is proposed, I am asking this Committee for its support in maintaining the special industry committee system for setting minimum wages in American Samoa.

#### **Conclusion**

I once again thank you Mr. Chairman, as well as your distinguished colleagues for the opportunity to speak here today. It is my fervent wish that you keep American Samoa's plight in your thoughts as you consider the budget of the Office of Insular Affairs for the new fiscal year.

*Soifua ma ia manuia.*

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Mrs. CHRISTENSEN. And now we will receive the testimony from The Honorable Felix Camacho, the Governor of Guam.

**STATEMENT OF FELIX PEREZ CAMACHO,  
GOVERNOR, GUAM**

Governor CAMACHO. Madam Chair, thank you. And members of this newly reestablished Subcommittee on Insular Affairs, I thank you for this opportunity to present my testimony today which will present Guam's view on the work of the Office of Insular Affairs and the support OIA has offered us, assisting us in the challenges that face the Government of Guam, and, of course, the role of the U.S. Department of Interior in our island's future as we enter a period of growth and extreme complexity.

I had a State of the Island address recently, and I mentioned that the island is growing stronger, our economy and the state of our island is strong. But despite that, we have many complex challenges that the anticipated increased military presence will bring. And I am confident that OIA will be of invaluable assistance as we partner with the Federal Government and DOD in this season of growth.

I also would like to express my appreciation to David Cohen, Nik Pula and other members of their staff of OIA. The Bush administration's proposal for Fiscal Year 2008 is roughly \$403.8 million for OIA. I believe it is a responsible budget, and one I believe will do much to ensure that the territories of the insular areas are able to further improve their respective government infrastructure and economic diversification. I believe it is in those two areas that we have really received much input.

As you know, Guam stands to benefit, of course, from the technical assistance programs to eradicate, as you mentioned earlier in your opening statements, invasive species like the brown tree snake. There has been very much success in the FMIP programs, the Financial Management Improvement Programs, with our Department of Administration and the technical assistance that has been provided. The protection of our ecosystems, and I believe most important is the hardening of our aging infrastructure systems is where the greatest challenge will be. I, of course, have submitted the testimony, so I think the record speaks for itself.

But Congresswoman Bordallo talked about—the question really was, what is it we are going to do in the anticipation of the build-up, you know, and others that it is going to be an extremely complex issue and of a magnitude we have never seen before. There is concern of its impact on the quality of life, of course, and our ability to keep pace with the military development.

Our desire is to ensure that the development is mutually beneficial. The challenge though, as we all know in the islands, is our ability, our financial capacity to provide for infrastructure; on top of that, the many demands placed upon us with other Federal agencies. There may be Federal mandates that are unfunded, EITC being one, consent decrees imposed upon us for the closure of a 60-year-old dump, and the requirement of the building of a new one, time management is not met, moneys that are not available, and an almost impossible situation, it seems, at times.

That, of course, all faced with the realization that as the U.S. realigns its forces throughout the world, the strategic importance and significance of Guam is becoming abundantly clear. I look at all of this as an opportunity, not a challenge, but really an opportunity



for us to work together. We have had the ability of working with OEA as an example, but Interior and the funding that is provided there is going to be extremely critical.

Our Port Authority is one area that definitely has not had or seen any type of improvement in its infrastructure for many years. It receives 95 percent of all the goods. There is a \$2 million loan or grant that would be provided to purchase an additional gantry crane. The impact on that not only in our local economy, but on the capacity and the need for the military or DOD to bring in their goods for growth and development is extremely highlighted.

So the challenges obviously remain—there are discretionary fundings that are provided to deal with various issues at OIA, including the compliance with the National Environmental Policy Act, the transition of the Department's financial and business management system.

Now, I mentioned earlier that the build-up of the U.S. military on Guam is underway. Aside from infrastructure, challenges that we face, of course, are going to be expected growth in population. I anticipate that over the next 10 years, we are going to see a 12 to 15 percent growth in our population, and the stresses placed upon it in health, education, public safety are going to be extremely highlighted. So along with that, we talked about the water, wastewater, power, transportation systems that have been identified, and there is a need to maintain and improve the current or future service levels.

As mentioned, because of our limited resources, individual agencies within our government continue to seek funding sources or availability. I have submitted a request to the Secretary of Interior to create an Interagency Group on Insular Affairs Working Group on Military Expansion. This would be in cooperation with the U.S. Department of Defense's Joint Guam Program Office, and I believe that a combination of these two groups would be extremely beneficial.

To put the notes aside, I also just wanted to talk briefly on your concept of a bond bank, which can be utilized in the territories as a vehicle for securing Federal guarantees for funding necessary to prepare for and support the military expansion on our island. I support this effort to pull the efforts of the territories together to seek bond financing for specific issues like infrastructure development. This bond bank would take much of the administrative work normally reserved for economic development authorities in our areas and would focus on working with borrowing communities or institutions to ensure that the most advantageous financing options are explored.

The bond bank is an attractive vehicle that is greatly needed for our investors and can certainly bring about the projected \$600- to \$800 million worth of needed improvements in our infrastructure as a whole, and I ask that the committee supports the territories in such an effort, and please know that this would greatly assist Guam as the military is building up on both ends of our island.

I am truly appreciative of all the efforts that have been provided, and as mentioned by my colleague, Governor Tulafono, this Subcommittee and our ability to talk to you directly on the issues that affect our islands I think is critical and much, much received.

The islands, in closing, always face the challenges of financing, and fragile economies that oftentimes our ability to deliver and provide for the quality of life and opportunities necessary for our people are extremely and greatly challenged. But by working with you and recognizing the uniqueness of island economies and governments, I believe that there are, as I mentioned, extreme opportunities to prosper. So I look forward to working with you, as mentioned earlier. The details of our testimony is provided here. But again, I believe that Guam stands to benefit from this, and the \$403.8 million budget for OIA I believe, again, is a responsible one, and would do much to ensure that the territories are able to further improve our economies, both in infrastructure and quality of life. So with that, I thank you very much for this opportunity.

[The prepared statement of Governor Camacho follows:]

**Statement of The Honorable Felix Perez Camacho,  
Governor of Guam**

Mr. Chairman and Members of the Committee, thank you for inviting me to participate in your hearing on the Fiscal Year 2008 Budget request for the Office of Insular Affairs, U.S. Department of the Interior, specifically its impact on the island of Guam for the coming year. My name is Felix Perez Camacho; I am the Governor of Guam. My testimony today is to present to you Guam's view on the work of the Office of Insular Affairs, the support OIA has offered in assisting us through the challenges that have faced the Government of Guam in providing basic services to our people, and the role of the U.S. Department of the Interior in our island's future as we enter a period of prosperity.

Mr. Chairman, I would like to express my appreciation to you and to the members of the Committee for holding this hearing to better understand the needs and concerns of the Pacific Island Territories on this most important issue for the people of Guam and our Pacific Island brothers and sisters.

Last week, I delivered my annual report on the State of the Island of Guam. It offered a synopsis of the challenges we currently face, offered up realistic solutions to get our island through what has been some tough financial times for the Government of Guam, and, most importantly, where we are headed in the next year and beyond. As I told my people and as I share with you here on Capitol Hill, the State of our island is growing strong and will grow even stronger. Despite the challenges that an increased military presence will bring, I am confident that the OIA will be of invaluable assistance as we partner with the Federal Government in Guam's Season of Transformation.

During my Administration I have been proud of the relationship that has been established between the Office, its management and the great people who work everyday with the Government of Guam to ensure that federal money spent on our island is done so wisely and with great attention to reporting its use back to Washington D.C.

I want to take this opportunity to commend Deputy Assistant Secretary of the U.S. Department of the Interior David Cohen for his leadership of the Office of Insular Affairs. Mr. Cohen has been such a staunch advocate for the people of Guam and it has been through his efforts that great progress has been made on our island in the areas of accountability and in the capital improvements made over the past four years.

Mr. Nik Pula and the staff of the Office of Insular Affairs have also been a tremendous help. Their vision is in line with ours to bring about lasting change to the programs we offer our people and to ensure that each dollar is protected and well spent for the betterment of the people of Guam.

It has been the commitment to following the mandates as set out by Congress and the unwavering support of the good men and women at the U.S. Department of the Interior that have changed the perception of Guam to one that is responsible in the administration of federal dollars and with a clear direction of where as a people and, as citizens of this great nation.

The Bush Administration proposal for FY 2008 of \$403.8 million for the Office of Insular Affairs (OIA) is a responsible budget and one I believe will do much to ensure that the Territories of the Insular Areas are able to further improve their respective government infrastructure and economic diversification.

There is no question that the programs funded under the FY 2008 Budget Request will continue to result in long-term benefits throughout the territories and Freely Associated States. I look with great interest in the more than \$200 million in Compact of Free Association Sector Grants that are included in the 2008 budget. Guam stands to benefit from the more than \$12 million in technical assistance programs to eradicate invasive species in the Western Pacific, strengthen the financial management of our governments, protecting our reef ecosystems and hardening our aging infrastructure systems.

There is one item of interest that this budget reflects and that is \$2 million to support the installation of an additional gantry crane at the Port Authority of Guam. The Port Authority of Guam owns, controls and manages just over 1,000 acres of fast and submerged lands comprising Cabras Island (CI), which is a heavy industrial area. The Sea port at Apra Harbor is the entry point for 95% of all goods entering the island, and is a transshipment center for Micronesia with over 20 cargo ships leaving outbound throughout the Western Pacific on a monthly basis. The port also sees 200 port calls by vessels carrying containers annually, accommodates over 27,000 cruise passenger arrivals, 5 million barrels of fuel, up to 100 fuel tankers, and 2,000 port calls by foreign fishing boats each year. This additional gantry crane will continue to allow us to reap the benefits of trade between the United States and Asia. It is critical to the further diversification of our economy through the Regional Distribution Center initiative I am committed to implementing. This compliments the Office of Insular Affairs mandate to improve the economies of our islands and, to expand our economic base so that we will be less reliant on the largesse of the Federal Government. OIA is committed to seeing this initiative occur and even supported it by providing with the initial grant for this project.

As the U.S. realigns its forces throughout the world, the strategic importance and significance of Guam is becoming abundantly clear. With the repositioning of U.S. forces and their dependents to Guam in the immediate years ahead, Guam's Port will be the first entity to feel and support the impact of this increase in the form of construction materials and goods. These materials are immediate and essential for the enormous buildup that will occur to accommodate our troops and their families. The Port of Guam will also see an influx of household goods and consumer goods as a result of our increased military population and their families. The \$2 million will contribute to a portion of the cost associated with the acquisition of a new gantry crane, which will assist immediately with the importation of construction materials related to the buildup of necessary.

The budget request also includes an increase in discretionary funding to deal with various issues at OIA including compliance with the National Environmental Policy Act and the transition of the Department's Financial and Business Management System. Just as the OIA has remained committed to promoting sound financial management practices in the insular governments, encouraging private sector-led economic development, and increasing Federal responsiveness to the unique needs of island communities, their budget must reflect that.

This request comes as word of the buildup of the U.S. Military is underway on Guam. With the increase of U.S. military assets to Guam expected over the next 10 years, the Government of Guam has begun the preparation to receive an estimated 8,000 to 12,000 military personnel and their dependents. According to U.S. Census Bureau estimates, Guam's population is expected to increase from 168,564 in 2005 to 180,692 in 2010, without factoring any increase to the local military population by the United States Department of Defense. The increases are enough to direct capital improvement in those locations expected to develop more rapidly in the expansion as identified by military planners.

The Government of Guam's 10-year Consolidated Infrastructure Improvement Forecast has determined that much of the infrastructure throughout the island, installed following the Liberation of Guam from Japanese occupation in 1944, needs to be completely replaced.

Other major water, wastewater, power and transportation systems projects have been identified to maintain or improve current and future service levels. The improvements to the junctions that adjoin military and civilian facilities have also been slated for improvement. Millions of dollars in capital improvement projects have been identified in the civilian community, though we continue to seek for more than half of those projects. Because of limited resources, individual agencies within the Government of Guam continue to seek funding sources, including bond financing, to support projects that will improve the quality of life for all residents. The Government of Guam is taking cost-cutting measures and approaches to maximize the limited funding opportunities afforded the island as a U.S. Territory void of natural resources.

I have already asked the Secretary of the Interior to create an Interagency Group on Insular Areas Working Group on Military Expansion. The U.S. Department of the Interior Office of Insular Affairs, in cooperation with the U.S. Department of Defense Joint Guam Program Office, would lead the group. The group would ideally include a number of federal government agencies and all relevant executive branch divisions of the agencies to guide the Government of Guam and the island's U.S. military commands in understanding what is needed to respond to this tremendous growth and the certain impacts to the Guam community now and into the future. I believe that proceeding on a monthly basis, the working group would help in the effort to address critical workforce needs and provide guidance in the completion of all expedited Capital Improvement Projects related to the military expansion in Guam.

This, in combination with funds from the U.S. Congress, public-private partnerships would also help the Government of Guam and Guam's military partners in securing the necessary funding to make the upgrades necessary in anticipation of the increase in U.S. forces in Guam and improve the quality of life for both residents and military personnel. This issue will be further worked out as the Government of Japan continues its efforts to assist with the \$10 billion investment into the military in the Western Pacific.

I believe that a bond bank can be utilized in the Territories as a vehicle for securing federal guarantees for funding necessary to prepare for and support the military expansion on our island. I support this effort to pool the efforts of the territories together to seek bond financing for specific issues like infrastructure development. A bond bank would take much of the administrative work, normally reserved for the economic development authorities in our areas, and would focus on working with borrowing communities to ensure that the most advantageous financing options are explored. The bond bank is an attractive vehicle for investors and can bring about the projected \$600 to \$800 million needed to improve our infrastructure as a whole. I ask that the Committee support the Territories in such an effort and please know that this would greatly assist Guam as the military is building up on both ends of my island.

#### Summary

Mr. Chairman and members of the Committee, Guam continues to move ahead together with our island brothers and sisters in Micronesia and the Western Pacific; but there is so much more that can be done to ensure that Guam stays on a course to prosperity. I share your values, your priorities and your concerns as leaders of our great Nation and today, I ask you to stand with the people of Guam as we take our island to new heights and to build a greater Guam better and stronger than we've ever seen and firmly establish Guam as the showcase of our democracy.

Thank you for your attention. I am pleased to answer any questions.

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Mrs. CHRISTENSEN. Secretary Cohen, welcome. We have just taken testimony from the Governors, so what we will do now is we will ask them some questions, and we will give you a chance to catch your breath, if that is OK with you. Thank you.

And the Chair now recognizes myself for 5 minutes of questioning, and I will start. Governor Camacho, at the end of his testimony spoke about the budget and feeling that it was a good budget. Governor Tulafono, in your testimony, you talk about the value of the Office of Insular Affairs in helping to promote economic development in the territory, and you underscore the importance of the technical assistance account, and your support for its continuation and expansion. So given your experience with having to compete with the other insular areas for technical assistance, have you given any thought to what level you think that technical assistance accounts ought to be funded at?

And if you have any comments, Governor Camacho, I would welcome yours as well.

Governor TOGIOLA. The technical assistance grant has been a great vehicle to back us up in areas where we are not able to provide funding for critical needs in terms of studies and affecting

some of the things that we need to promote ourselves. However, the efforts are limited only by the fact that the fundings are limited.

I don't know exactly how much would be adequate, but I do believe that in order to adequately address the needs, which there are abundant from all the insular areas, that an extension of that program is truly required.

Mrs. CHRISTENSEN. Governor Camacho, did you have any—

Governor CAMACHO. Certainly. Is there ever enough? No. And I think our challenge has always been recognizing that it is a limited pool of resources that is competitive. How can we maximize these technical assistance grants? And I believe that one area that we have been successful, and I am very much appreciative of this technical assistance and the grants, has been in the Financial Management Improvement Projects for the government. Both hardware and technical assistance has enabled us, at least in the Department of Administration, to get a better handle on our finances to certainly upgrade the infrastructure in that area, and I see a need to expand greatly.

I believe that with innovation and technology, we can improve efficiencies, and this is not just in the financial management of our accounts, but certainly in the reporting requirements and data necessary that is required as grant moneys are given. So reporting is certainly there.

Efficiency improvements in the area of health care, in public safety and education are areas that I think with assistance grants, that if we can improve on those areas, it certainly has long-lasting impacts that are extremely beneficial.

As you know, we have received grant moneys also for invasive species, and although it may be—it may seem that the brown tree snake doesn't have—it may be a joke, it seems, outside of Guam, the impact it could have on neighboring islands and their fragile tourism economies, even the State of Hawaii and the impact on agriculture and livestock, it is tremendous. So when you think about also the grants provided for our ecosystems upon which our tourism industry depends on is very real.

The one area that we fall short of, I believe, is the hardening of our aging infrastructure systems, and I talk about water power, wastewater systems that are absolutely mandatory, necessary. That is where the challenges are. And as I mentioned earlier, with this bond bank as a financing vehicle, we need to be creative in finding ways for the territories to seek additional funding outside of the normal channels. It is always going to be a challenge for us in finding ways to pay for it, and the ability of the local governments with restricted and limited budgets to pay for multimillion-dollar improvements is always going to be very real and very, very complex. Thank you.

Mrs. CHRISTENSEN. Since I am almost out of time, I will come back on another round with some of my further questions.

At this point I will yield to the Ranking Member Mr. Fortuño for 5 minutes.

Mr. FORTUÑO. Thank you, Madam Chairwoman. I commend you for the hearing we are having today, and I want to thank both Governors for your testimony.

You both talked about the challenges the territories face. Perhaps we have an 18th century solution to 21st century issues, and that is what we are dealing with, and we are fully cognizant of that fact over here on the dais as well.

If I may start with Governor Tulafono, you mentioned actually report language on the tax package that was extended for another 2 years, and actually that report language is very explicit, I would say, in terms of promoting that nontax policy alternatives be explored for any long-term economic development policies toward the possessions. And actually I believe that is the mood of Congress regardless of who is in the Majority or in the Minority. That is my feeling here.

And you mentioned and stressed how important maintaining the special industry committee processes for setting minimum wage standards are. Could you expand further on those needs regarding those special industry committee processes, please?

Governor TOGIOLA. We support the continuation of the special committees because we believe the committees have been very responsive to the local conditions and the local situations. Imposition of minimum wages that are conducive to economic conditions in the United States are definitely not going to now work for American Samoa, and the structure of this committee is such that an economic study is done before the hearings. Our input is given as a local government from a government's point of view, and then the participation of our community and the Federal Government in the process of the committee itself lends for a very well-supported investigation of whether or not, you know, increases in the wages are justifiable.

And I will say that ever since I have been involved with the process, I found the committees to be very responsive to real situations and to the real conditions of American Samoa, and their decisions have been conducive to the supporting of the committee and what they do. So in that regard, we believe that it is the only thing that has proven to work for our situation at this point in time. Perhaps in the future there might be some other process that may work better, but for now, this is the thing that has been proven to work best for us. So we would urge your support in continuing that for American Samoa.

Mr. FORTUÑO. I understand.

Governor Perez Camacho, if I may, certainly this increase in the number of military personnel in the next couple of years will create some stress on the infrastructure, as you were mentioning, of Guam. Could you expand a little bit further as to different examples of what you all are doing in preparing for the arrival of the personnel and their dependents and all the assets that will be there?

Governor CAMACHO. Thank you very much. Our Census Bureau estimates that our population is expected to increase from roughly 168,000, which was in 2005, to roughly 180,000 by 2010. When you add military personnel, an anticipated 8,000 to 12,000 Active Duty, and when you throw in the support personnel and family members, it could be anywhere from a total of an additional 17,000 to 24,000 personnel by 2014. So between 8 and 10 years from now, I think

we can see that the population will grow between 12 and 15 percent.

In anticipation of that growth, we are working closely with the Office of Economic Adjustment, or OEA, working, of course, with the Department of Interior, and ensuring that we have to improve—we are going to be developing a master plan that would cover infrastructure, water power, wastewater, all the infrastructure needs. We have also got a group together that is focusing on the social impact for, of course, public safety, education and public health. And by recognizing that we have to approach this in a very deliberate and phased process, by developing a master plan that would transcend administrations, recognizing I will be gone in 4 years and the new Governor will be there and legislature and other leaders, a plan must be implemented, backed up by an organization that will transcend politics and be there for the duration. We then have to back this up with adequate funding.

The government to this day actually is still challenged in the U.S. Supreme Court by a case that was brought against my administration from the now removed attorney general. We are anticipating a decision by June on our ability or authority to borrow on the bond market anywhere up to \$250 million, but that is just for debt. The challenge will be how do we pay for infrastructure that can be mutually beneficial to our civilian community and allow for growth on the military end? We think that there are opportunities there, but by working with OEA, by working with Interior, by working with the Department of Defense and finding creative ways through public-private partnerships, we can find ways to fund it, but it is going to be a very, very deliberate, very well thought out and complex issue. Something of this magnitude has never been seen on Guam since World War II when we had to recover from the effects of the Japanese invasion and, of course, liberation by U.S. forces. So it is of that magnitude.

So it is with those efforts that we are going to proceed in a very deliberate manner. But again, the challenges are, once we have that master plan, finding a way to pay for it will be the biggest challenge.

Mr. FORTUÑO. Thank you. And I am sorry we went over time.

Mrs. CHRISTENSEN. That is all right.

The Chair now recognizes Ms. Bordallo for 5 minutes.

Ms. BORDALLO. Thank you, Madam Chairman.

First of all, Governor Camacho, thank you for your comments on the bond bank. I do agree with you and the military build-up. It is an opportunity. And there are challenges, and I think working together, we are going to be able to survive all of the challenges.

I have one question here for you. Is the reconciliation process for Section 30 funds adequate from your standpoint? And are the Federal agencies forthright in reporting Section 30 funds that are owed to Guam?

Governor CAMACHO. We recently had a Director of Taxation working out here with, I believe, the relevant agencies that are there. We have been able to go back, I think, to the mid-1980s to rectify some of the discrepancies and make some corrections there.

I believe there is room for improvement in the way of reporting, in the way of accuracy of data and information. It has been an

ongoing process, but I think we are getting there. Through better communication and better data, I think we can begin to reconcile and ensure that we do collect on the Section 30s.

But if I may just digress a bit and indicate that the real challenge we face right now is with Department of Defense contracts for construction and business that is being conducted on Guam. We need to find ways to ensure that corporations that come and do Department of Defense work on the island are properly registered, and they pay their fair share in taxes. A billion dollars' worth of construction has occurred over the last 4 or 5 years, and without Guam being able to collect. I think we were able to collect out of the amount of money owed roughly \$4 million, or rather \$40,900,000. So you can see that there is a real shortfall in that area, but by better cooperation with DOD and our taxation department, we can work on it.

Section 30, though, there is room for improvement, but I see that there has been collaboration.

Ms. BORDALLO. So what you are saying then to the committee, Governor, is you will continue to monitor this, correct?

Governor CAMACHO. Yes.

Ms. BORDALLO. All right. I have another question. Does the government in Guam have a process for clearing open items in the Inspector General's reports? By this, I think these open items are financial accountability, audit reports and that type thing. Is OIA helpful in working with you to clear the open items?

Governor CAMACHO. I believe that they are. With the technical assistant grants that have been given, particularly in the area of our financial management improvement plans through Department of Administration, our ability to improve upon our accounting procedures has greatly improved. There have been a certain number of qualifications; I would say on average about 11. We have reduced to down to about one or two, so we have made tremendous progress in that regard.

Ms. BORDALLO. Governor from American Samoa Tulafono, do you feel Insular Affairs has been responsive to your request for technical assistance?

Governor TOGIOLA. I believe they have, and I think one of the classic examples of that success and one of the, I think, finance success stories is the fact that when we came into office, American Samoa was about 8 years behind in their financial statements, and where—

Ms. BORDALLO. Did you say 8 years or 80?

Governor TOGIOLA. Eight. I am sorry. I am still recovering from a cold. I could say 80 because that would just make me look better.

But we asked the Department of Interior for assistance, and through the technical assistance and other OMIP and FMIP grants, we were able to put together the financial system and the financial mechanisms that has brought us current to date with our financial statements. And without that technical assistance and the assistance from OIA and the Department of Interior, it might have never been possible for us to bring our financial information and our financial statements current as it is today.

And I believe also the success of the business conferences are beginning to yield results, and in addition to that, they are also



helping us with our own local promotions, efforts where they would allow technical assistance funds to allow our Department of Commerce to do their own promotions in promoting our economic development.

Ms. BORDALLO. Perhaps you have more or less answered this, but I will ask it. In 2002, the American Samoa Economic Advisory Commission submitted a report entitled Transforming the Economy of American Samoa. As you know, the Commission was the first of its kind in American Samoa's history to specifically address the economic needs of American Samoa. To what extent has the report assisted you in laying out a vision for the economic diversification in American Samoa?

Governor TOGIOLA. Well, before I give an opinion, response to your question, ma'am, I should preface my response by saying that I was one of the Commissioners, so if my response is slightly biased, there is a good reason for that.

I believe the report of the Governor Waihee Commission that was commissioned by the Department of Interior had provided us a great document that provided good guidelines for what we needed to do. Even though we have had a long dialogue about that and what to do with it, our administration has gone forward and begin to implement changes along the lines of the recommendations provided by the Commission. So every now and then we have some agreements on some of those things. And we have also been able to utilize that document to support technical assistance requests.

Ms. BORDALLO. Good.

Governor TOGIOLA. And to some degree, we have received some assistance to implement some of those things on a local level.

Ms. BORDALLO. Thank you. Thank you very much, Governor.

I yield back.

Mrs. CHRISTENSEN. Thank you.

I am going to recognize myself for another round. And if the other Members have other questions, we will recognize them as well.

Governor Tulafono, I wanted to follow up on that question. And you talked a lot about the need for a plan, and I was wondering what is the relationship of that Commission's plan, the report, to your need for a plan, and are you required—would you require more assistance from OIA for the development of that plan, or is it something that you think American Samoa can do on its own?

Governor TOGIOLA. I think this is, Madam Chairlady, something that is not necessarily related to the American Samoa Economic Advisory Commission report. What I talk about today is something that will help us deal with the shifts and changing in the national policies, trade agreements, issues of minimum wage increases, the loss of tax credits and the withering away of the benefits of headnote 3A as it relates to trade agreements and all that.

What I am talking about is, I believe, that funding for—at least for American Samoa should be done within the context of a plan where funding sources are identified much like what, you know, the United States does with compact states, where you know what you are going to get, and you know what you can plan for that, and we will give you a direction for the long term instead of just a year by year by year. As it is, as much as we appreciate the funds that

we receive, it is very tough to plan. It is very tough to plan replacing the infrastructure from—you know, in this fashion.

So what I am talking about is maybe through the process of your Subcommittee and the necessary parties, us, the Interior and who else there may be, so that we can look at all the policies of the United States and say, this is the best direction for the territory that we will assure that no matter what the policy shifts will be, that there is consistency. As it is today, we cannot market American Samoa meaningfully because of their minimum wage issue, because of the lack of Federal incentives. So that is what I am talking about today, ma'am.

Mrs. CHRISTENSEN. I understand it better now.

And just to follow up on another issue that was raised by Governor Camacho, and it is also included in Governor Tenorio's written statement, on their support for the bond bank. Do you also support that concept?

Governor Camacho, you recently noted in your State of the Island address that the island of Guam has a \$700 million deficit. Could you tell the Subcommittee what steps have been taken to address that growing deficit over the last 2, 3 years, and do you see the Federal Government in having any role in Guam's financial problems.

Governor CAMACHO. As a matter of record, the deficit is at \$511 million. When I had stepped into office in 2003, we inherited a deficit of \$209 million. What has added to it has not been so much an operational deficit, but rather several judgments and settlements that have occurred in our courts, the biggest being the most recent \$123 million judgment against the government for a retirement bonus, if you will. It is a 13- or 14-year-old law—or case that had been filed and was finally dealt with by a certain judge and made a ruling against the government. It is, again, a judgment that would have to be funded by the local general fund, totally unanticipated.

The other significant addition to the deficit has been a \$90 million settlement on the earned income tax credit that remains unpaid after roughly 8 years, dating back to 1996. That, again, is another settlement that has to be paid out of the general taxes or the general fund of our government. It is another typical example of the—you know, the round peg going into a square, or square peg going into a round hole. It is an unfunded Federal mandate that the territories have a very difficult time, and now it has a major impact upon our finances.

So those are the two issues that have added greatly to it.

And finally, I would have to say that the \$700 million figure is what I indicated that in the next 5 years, should we not—or should our local policymakers or legislature not implement what I am going to be presenting, which is a deficit elimination and fiscal recovery plan, should they not follow it and implement it as we proceed in the 2008 budget over the next 5 years, it could potentially grow to that amount. So there is a sense of urgency and a need for fiscal discipline in that area.

Mrs. CHRISTENSEN. The Chair will now recognize Mr. Fortuño for a second round.

Mr. FORTUÑO. Thank you again, Madam Chairwoman.

Actually, going back to each of the two local economies and the concerns that you raise—certainly you are both trying to do the best you can given the circumstances—brings to my recollection actually a great piece that was put together by a university professor. He is of Chilean descent. His name is Fernando Lefort. He wrote about how in colonial times, colonial colonies, economies diverted from the country's—you know, the mother country's economy in such a way that is very similar to what occurs between the economies of territories and the U.S. economy. And there are different reasons for it, and actually, if I may, we will get it, and if we have a few days to put it into the record, I appreciate that.

Mrs. CHRISTENSEN. Without objection, so ordered.

**[NOTE; The report entitled "PUERTO RICO'S ECONOMY IS NOT CATCHING UP" by Fernando Lefort, Business School, Pontificia Universidad Católica de Chile submitted for the record has been retained in the Committee's official files.]**

Mr. FORTUÑO. Thank you.

Going back to that issue again, again, the issues, for example, Governor Tulafono, you bring to our attention are very familiar: trade agreements, our opening of markets that previously were almost exclusive to U.S. territories, the fact that the tax policies have changed and those benefits are no longer there, the increases in the cost of operating vis-a-vis the cost that could be borne in the mainland and so on and so forth. What—if you would discuss very briefly, which way—you mention at the end Internet-Based and knowledge-based, specialized industries perhaps. Is that the way American Samoa will be going? Is that how you feel you will be going?

Governor TOGIOLA. Just reflecting back on the historical successes of Section 936, after 50 years, we have only really had two companies that took advantage of that and located plants in American Samoa. I do not think it really is going to do anything further for us.

The fiberoptic cable was brought to the fore as a result of the investigation of business opportunities and where a certain company came in and wanted to establish call centers on the islands, but after their investigation of the satellite capability and telecommunication capability, they determined they cannot do that kind of business unless there is fiberoptic.

From that point forward, we have gone forward, full steam ahead, in doing that because we have also been consulted by banking institutions. They would like to relocate certain banking products into American Samoa because of the favorable business atmosphere, but they cannot do it with satellite communications.

So, after listening to those two discussions, we made the determination that if we are going to be able to diversify, invite new businesses different from the canneries and truly achieve diversification of the economy, the fiberoptic is the link that is necessary; and that is why we are asking for your assistance in this endeavor.

Mr. FORTUÑO. If I may ask very briefly and quickly, what percentage of the total workforce is tourism and what percentage is government employees in both Territories?

Governor TOGIOLA. In American Samoa, tourism is not a very well developed—

Mr. FORTUÑO. OK.

Governor TOGIOLA.—industry. We are doing some things together with the assistance of the Department of Interior to develop the infrastructure for tourism, but one of the biggest challenges that we have is transportation. Transportation is extremely expensive and erratic, and you cannot develop, you know, meaningful tourism unless you have consistent, reasonably priced air transportation. We do not have that. It is an issue with us before the Department of Transportation right now.

Mr. FORTUÑO. And how big is the government vis-a-vis the general population, the working population?

Governor TOGIOLA. Our employable workforce is estimated around 18,000. Unfortunately, the most recent figures that have been presented to us show that the aggregate unemployment rate in American Samoa is 29 percent. Of course, that percentage includes people—farmers, subsistence farmers, who sell their products in the markets and are self-supporting in that regard, who may not be employed, but they earn income through different sources. So, while it says 29 percent, our local estimate is around 16, 17 percent.

Mr. FORTUÑO. OK. Thank you.

May I have Governor Perez Camacho answer very briefly about what percentage is government and what percentage is tourism?

Governor CAMACHO. With the total workforce right now, the government has, roughly, between 11,000 to 12,000 employees. A small percentage of that is Federally funded, but the majority of our workforce is in the private sector, and as a parallel comparison, the economy is 60 percent funded by tourism, 30 percent funded by military and 10 percent, roughly, by the service industry.

We have an unemployment rate of about 7 percent. It has been slashed by half. When I entered office, it was about 14. So there has been dramatic improvement in that area.

Mr. FORTUÑO. Thank you both.

Mrs. CHRISTENSEN. Thank you.

The Chair recognizes Ms. Bordallo for a second round.

Ms. BORDALLO. Thank you, Madam Chairman. I do have some questions for Mr. Cohen. We are going to be able to—

Mrs. CHRISTENSEN. Yes. Yes.

Ms. BORDALLO. This one is for Governor Camacho.

In your State of the Island address, Governor, you also stated that you cannot adequately exercise sufficient management of the entire government of Guam.

Can you give us a sense of the additional authority that you would need to address these concerns? And do you think the Organic Act should be amended further to strengthen the authority of the Governor?

Governor CAMACHO. Well, that is—thank you—a very, very intriguing question and a very, very important question. I thank you for asking that.

I had noticed prior to being Governor—I had a 10-year career as a senator. I was a local legislator, and through the years there has been an erosion of the organic authority of the Governor by local

legislation. I think the Organic Act is written in a very broad sweep, and there is a provision that would allow for local interpretation in the very broad areas. However, the local legislature has begun to erode that.

For example and specific to your question about my authority to manage specifically the cash management of our government, in the area of our public school system, which clearly utilizes in excess of—more than half of our revenues go toward education, local legislation has established an elected body which then chooses its superintendent.

But by budget law, they have required that a section of our revenue, which is withholding tax—first, it began with 82.5 percent goes toward education; we found out it was insufficient. Then they improved it to 100 percent of withholding taxes will then go to education; they found out that that still was not sufficient. Then they said, you now must give all withholding tax and anything else needed, and you must give it to education first before you can pay anyone else.

And so, if I may use an analogy, it would be like a family that is at the table having a meal, and you have a very robust and healthy child who may be slightly overweight, and the father says, “That child will eat everything on this table until he is satisfied, and whatever is left over, the rest of you can eat.” so my authority has been taken.

If I can further explain, between Fiscal Year 2004 and 2005 in the line agencies that I have controlled with casual management, we have reduced expenditures by \$11.1 million between 2005 and 2006 with the line agencies that I, again, control; and with the cash allotment, I have reduced it by 12.2, and yet, our education department has gone extremely overboard.

If I cannot control more than 50 percent of the cash flow of government which goes toward education, then I lose control, and we have a growing deficit. I do intend to take a look at my own organic authority and see if it has been violated and, perhaps, bring this to court.

Thank you.

Ms. BORDALLO. Thank you, Governor.

Mrs. CHRISTENSEN. Thank you.

You know, I am just getting used to being a chairwoman. I cut myself off right at the 5 minutes, but I did have one further question to Governor Camacho which follows what you just spoke about and also your statement earlier about the need for fiscal discipline.

There are a lot of similarities between Guam and the U.S. Virgin Islands, and as you, I am sure, know, I have introduced legislation to create a chief financial officer for the Territory, which would be a person who would be chosen locally, nominated by the Governor, confirmed by the local legislature; and that person would have the responsibility for certifying revenues and ensuring that we do not overspend in any area or overall.

We heard from the Inspector General last week and from someone from the General Accountability Office who had been looking at issues in Interior and in the Territories, and they both supported the concept of a CFO.

Do you think that would be something that would be helpful for Guam?

Governor CAMACHO. I believe it would be, but it must be balanced against the existing legislation that through the years continues to grow certain pieces of legislation. As it relates to cash allotment and cash management, it would have to be repealed, and I think, if you can find that balance, certainly it would work.

What the local legislature has attempted to do, to lend credibility to their efforts for funding education, is to engage and authorize our public auditor to certify the expenditure levels, and then it approves, of course, the releasing of funds. In violation of that very law, we have had to give more just so they can make payroll. So, in many ways, there is the use of the Office of Public Auditor as a chief financial officer, but I certainly would appreciate that. We do have our director of administration that serves in that role and capacity anyway right now.

Mrs. CHRISTENSEN. Thank you.

If it is OK with the other members of the committee, Deputy Assistant Secretary Cohen, I think, just got off a plane at around 6:00 o'clock this morning. We really appreciate your making that extra effort to be here, and we recognize you now for your testimony.

**STATEMENT OF DAVID B. COHEN, DEPUTY ASSISTANT SECRETARY FOR INSULAR AFFAIRS, U.S. DEPARTMENT OF THE INTERIOR**

Mr. COHEN. Thank you very much, Madam Chairwoman.

Mrs. CHRISTENSEN. Governors, would you like to be excused or are you fine?

OK. Thank you.

Go ahead, Mr. Cohen. I am sorry for the interruption.

Mr. COHEN. Thank you, Madam Chairwoman.

First, let me express my appreciation to the new leadership of this Congress and of the House Resources Committee for seeing fit to reestablish a Subcommittee on Insular Affairs. I think it is an excellent step, and I very much look forward to working with all of you.

Madam Chairwoman, we would like to thank you and the entire committee for the support that you have provided to the insular areas by funding economic development initiatives, critical infrastructure and technical assistance projects, which provide invaluable resources to the insular areas. OIA's top two priorities for the insular areas are to promote private-sector economic development and accountability for the Federal financial assistance that we provide to the insular areas. We discuss our specific efforts to make progress in these areas later in the testimony, but will begin with an overview of the proposed budget.

The Fiscal Year 2008 budget seeks to continue efforts to promote economic sustainability throughout the Territories and the freely associated states. The proposed Fiscal Year 2008 budget is \$403.8 million of which \$79.8 million is requested in current appropriations. With enactment of the Fiscal Year 2007 joint resolution, we now have a full-year current appropriation of \$81.5 million. Based

on the direction of the joint resolution, we are preparing a detailed operating plan for Fiscal Year 2007.

OIA's budget is broken out into two major categories of funding—permanent and mandatory and current discretionary. Most of OIA's budget reflects mandatory commitments to U.S.-affiliated insular areas and has permanently appropriated \$324.1 million. With current appropriations, two activities are considered to be mandatory—covenant grants, \$27.7 million, that provide for capital improvement projects, or CIP, in the U.S. Territories; and an annual health and education block grant given to the Republic of Palau in the amount of \$2 million.

This budget request includes a discretionary increase totaling \$560,000. This includes an additional \$200,000 to ensure compliance with the National Environmental Policy Act, NEPA, on Federally funded infrastructure projects, \$352,000 to fully fund fixed costs, and \$8,000 for the transition to the Department's financial and business management system.

The Fiscal Year 2008 OIA budget continues to focus on increasing self-sufficiency of insular areas. OIA will continue to provide assistance to develop more efficient and effective government in the insular areas through the Technical Assistance Program. This assistance includes grant funding that meets a variety of needs, including resources for critical infrastructure like wastewater systems, hospitals and schools.

In Fiscal Year 2006, OIA received over \$81 million in assistance to Territories' funding, providing over 90 percent of these funds to insular areas in the form of financial assistance grants and will continue this effort in the future. The 2008 request is \$79.8 million.

American Samoa operations in the amount of \$22.9 million, the second largest budget activity, is part of OIA's discretionary funding, but the requirement to provide funds is included in authorizing language. These funds provide essential assistance to the American Samoa government to provide basic services of health care, education, public safety, and support for the judiciary.

While not officially considered a mandatory program, Federal Services assistance—that is, \$2.9 million—is comprised of two sub-activities that were negotiated and defined in law. The first is reimbursement to the U.S. Postal Service for continuation of mail service to the Freely Associated States. Failure to provide this service would be a breach of the negotiated compact. The second activity provides funding for the Republic of Palau to conduct an annual financial audit. The only funding that can be considered truly discretionary are OIA salaries and expenses and the technical assistance activity, \$16.1 million, which account for \$24.3 million out of a total OIA budget of over \$400 million in Fiscal Year 2008.

It should be noted that all but 2 percent of the total funding received by OIA goes toward assistance to the Territories and to the Freely Associated States.

One of OIA's top two priorities, as noted above, is to help the insular areas expand and strengthen the private sectors, building more sustainable economies to meet the needs and aspirations of their citizens. Most of the economies of the insular areas are currently dominated by the public sector and cannot be sustained without significant subsidy from the Federal Government.

OIA has historically provided financial and technical assistance for a number of activities that can help strengthen the foundations for economic development, such as developing public infrastructure, improving health care, improving education, and providing expert analysis on issues affecting the economy. More recently, however, OIA has recognized the need to more directly facilitate private-sector economic development. OIA now makes it their priority to provide technical assistance to help the insular areas identify and implement the necessary steps to make their economies more sustainable.

For example, OIA has provided technical assistance in recent years to help the insular areas identify their competitive advantages, identify industries that have the most potential for success in bringing prosperity to the insular areas, identify companies in those industries that might consider investing in the insular areas, identify specific investment opportunities for those companies, reach out to as many of those companies as possible, educate companies on the competitive advantages offered by the insular areas, and assist insular area governments to identify and implement ways to make the insular areas more attractive to private-sector investment.

OIA has worked to find ways to make progress and economic development without a large commitment of resources. In fact, less than 1 percent of the assistance to Territories' appropriation is spent on private-sector development due to the fact that many of the costs of the major events in this program are borne by the participants. This effort is proving to be successful with business opportunities being fostered in the insular areas through OIA's facilitation efforts.

OIA's other top priority is to promote accountability in the insular areas for the Federal funds that we provide there. Specifically, OIA has been working with all of the Territories and the Freely Associated States to help the island governments improve financial policies and procedures, upgrade automated financial management systems, train staff, complete accurate financial statements, and meet Single Audit Act requirements.

At the start of this comprehensive effort, all of the insular areas were several years behind in completing financial statements in annual audits. At the same time, the insular areas have significantly improved their submission times for the annual audits. At this time, the insular areas have improved their timeliness. OIA will continue to assist the insular areas as they work toward compliance with the Single Audit Act.

In conclusion, we believe that this budget request supports the continuation of programs to help the insular areas attain self-sufficiency. Toward this ultimate goal, we are committed to promoting sound financial management practices in the insular area governments, encouraging private-sector-led economic development, increasing Federal responsiveness to the unique needs of the island communities.

We thank you for your continued support of the insular areas as you are considering OIA's 2008 budget request.

Thank you.

[The prepared statement of Mr. Cohen follows:]



**Statement of David B. Cohen, Deputy Assistant Secretary of the Interior  
for Insular Affairs**

Madam Chairwoman and members of the Committee, thank you for the opportunity to testify on the Fiscal Year 2008 Office of Insular Affairs budget request. As Deputy Assistant Secretary of the Interior for Insular Affairs, I am the Federal official that is responsible for generally administering, on behalf of the Secretary of the Interior, the Federal Government's relationship with the territories of Guam, American Samoa, the U.S. Virgin Islands, and the Commonwealth of the Northern Mariana Islands, as well as administering the financial assistance provided to the Freely Associated States (the Federated States of Micronesia, the Republic of the Marshall Islands, and the Republic of Palau) under the Compacts of Free Association.

Madam Chairwoman, we would like to thank you and the entire committee for the support you have provided to the insular areas by funding economic development initiatives, critical infrastructure, and technical assistance projects which provide invaluable resources to the insular areas. OIA's top two priorities for the insular areas are to promote private sector economic development and accountability for the Federal financial assistance that we provide to the insular areas. We discuss our specific efforts to make progress in these areas later in the testimony, but will begin with an overview of the proposed budget.

**Overview of the FY2008 Budget Request**

The FY 2008 budget request seeks to continue efforts to promote economic sustainability throughout the territories and Freely Associated States.

The proposed FY 2008 budget is \$403.8 million, of which \$79.8 million is requested in current appropriations. With enactment of the FY2007 Joint Resolution, we now have a full year current appropriation of \$81.5 million, not including additional funds that will be provided for 50 percent of the January 2007 pay raise. Based on direction of the Joint Resolution we are preparing a detailed operating plan for FY2007. We are not at liberty to disclose the details of the operating plans until they are approved by the Administration and submitted to Congress on March 17. At that time we will be able to provide comparisons at the program level with the 2008 budget request. The comparisons in our 2008 budget are with the third 2007 continuing resolution, which was in effect through February 15. Throughout this testimony the comparisons will be on that basis.

Over \$200.0 million in Compact of Free Association sector grants are included in the 2008 budget. More than \$12.0 million is requested for a variety of technical assistance programs, including ongoing efforts on Brown Tree Snake control, insular management controls, coral reef conservation, maintenance assistance, and water and wastewater projects. The 2008 budget request funds \$27.7 million in critical infrastructure projects including: \$3.0 million to support the development of an under-sea fiber-optic link to American Samoa, \$3.7 million to support the closure of the Puerto Rico Dump on Saipan, with the area being redeveloped as a public park, \$2.0 million to support the installation of an additional gantry crane at the Port of Guam, and \$2.8 million to support wastewater collection system upgrades throughout the U.S. Virgin Islands.

OIA's budget is broken out into two major categories of funding—permanent or mandatory and current discretionary. Most of OIA's budget reflects mandatory commitments to U.S.-affiliated insular areas and is permanently appropriated (\$324.1 million). Within current appropriations, two activities are considered to be mandatory: covenant grants (\$27.7 million) that provide for capital improvement projects (CIP) in U.S. territories and an annual health and education block grant given to the Republic of Palau (\$2.0 million).

This budget request includes a discretionary increase totaling \$560,000. This includes an additional \$200,000 to ensure compliance with the National Environmental Policy Act (NEPA) on Federally funded infrastructure projects, \$352,000 to fully fund fixed costs, and \$8,000 for the transition to the Department's Financial and Business Management System.

The FY 2008 OIA budget continues to focus on increasing the self-sufficiency of insular areas. OIA will continue to provide assistance to develop more efficient and effective government in the insular areas through the Technical Assistance Program. This assistance includes grant funding that meets a variety of needs, including resources for critical infrastructure like wastewater systems, hospitals, and schools. In FY 2006, OIA received over \$81.0 million in Assistance to Territories funding, providing over 90 percent of these funds to insular areas in the form of financial assistance grants and will continue this effort in the future. The 2008 request is \$79.8 million.

American Samoa Operations (\$22.9 million), the second largest budget activity, is part of OIA's discretionary funding but the requirement to provide funds is included in authorizing language. These funds provide essential assistance to the American Samoa Government to provide basic services of health care, education, public safety, and support for the judiciary.

While not officially considered a mandatory program, Federal Services assistance (\$2.9 million) is comprised of two subactivities that were negotiated and defined in law. The first is reimbursement to the U.S. Postal Service for continuation of mail service to the Freely Associated States. Failure to provide this service would be a breach of the negotiated Compact. The second activity provides funding for the Republic of Palau to conduct an annual financial audit. Public Law 99-658 provides that the Republic of Palau's single audit, in accordance with the Single Audit Act of 1984, will be conducted at no cost to Palau through FY 2009.

The only funding that can be considered truly discretionary are OIA salaries and expenses (\$8.2 million) and the Technical Assistance activity (\$16.1 million), which account for \$24.3 million out of the total OIA budget of \$403.8 million in FY 2008. It should be noted that all but two percent of the total funding received by OIA goes toward assistance to the territories.

### **Strengthening the Private Sector**

One of OIA's two top priorities, as noted above, is to help the insular areas expand and strengthen their private sectors, building more sustainable economies to meet the needs and aspirations of their citizens. Most of the economies of the insular areas are currently dominated by the public sector and cannot be sustained without significant subsidy from the Federal government. OIA has historically provided financial and technical assistance for a number of activities that can help strengthen the foundations for economic development, such as developing public infrastructure, improving health care, improving education, and providing expert analysis on issues affecting the economy.

More recently, however, OIA has recognized a need to more directly facilitate private sector economic development. OIA now makes it a priority to provide technical assistance to help the insular areas identify and implement the necessary steps to make their economies more sustainable. For example, OIA has provided technical assistance in recent years to help the insular areas identify their competitive advantages; identify industries that have the most potential for success in bringing prosperity to the insular areas; identify companies in those industries that might consider investing in the insular areas; identify specific investment opportunities for those companies; reach out to as many of those companies as possible; educate companies on the competitive advantages offered by the insular areas; and, assist insular area governments to identify and implement ways to make the insular areas more attractive to private sector investment.

The Island Fellows Program has been an important part of OIA's efforts to promote private sector economic development in the insular areas. Launched in 2003, the program sends graduate students from business schools such as Wharton, Harvard, Kellogg, and Georgetown to the insular areas to study their economies, identify competitive business advantages, identify industries that could be successful in the insular areas, identify investment opportunities for businesses in the insular areas, facilitate outreach to announce opportunities to mainland companies, and identify ways to improve the business climate. The work of the Island Fellows has supported the year-round efforts of OIA full-time staff and contractors in all of these activities. The Island Fellows also helped OIA organize conferences in 2003, 2004, and 2006, as well as three separate Business Opportunities Missions in 2005 and 2006, which gave island business and government officials the opportunity to meet and market opportunities to businesses from around the country. In 2006, the Island Fellows prepared private sector assessment reports for American Samoa, Guam, the U.S. Virgin Islands and the Commonwealth of the Northern Mariana Islands, following methodologies that the Asian Development Bank has used to produce similar reports for the Freely Associated States. These reports have received a great deal of attention in the insular areas, and are available on OIA's web site. In the coming year, the Island Fellows program will continue to focus on assisting with preparations for the fourth Conference on Business Opportunities in the Islands, which will be held in Guam in the Fall of 2007.

OIA has worked to find ways to make progress on economic development without a large commitment of resources. In fact, less than one percent of the Assistance to Territories appropriation is spent on private sector development, due to the fact that many of the costs for those major events are borne by participants. This effort is proving to be successful, with business opportunities being fostered in the insular areas through OIA's facilitation efforts.

### **Promoting Accountability**

OIA's other top priority is to promote accountability in the insular areas for the Federal funds. Specifically, OIA has been working with all of the territories and Freely Associated States to help the island governments improve financial policies and procedures, upgrade automated financial management systems, train staff, complete accurate financial statements, and meet Single Audit Act requirements. At the start of this comprehensive effort all of the insular areas were several years behind in completing financial statements and annual audits. At this time the insular areas have significantly improved their submission times for the annual audits. OIA will continue to assist the insular areas as they work towards compliance with the Single Audit Act.

### **Conclusion**

In conclusion, we believe that this budget request supports the continuation of programs to help the insular areas attain self-sufficiency. Towards this ultimate goal, we are committed to promoting sound financial management practices in the insular governments, encouraging private sector-led economic development, and increasing Federal responsiveness to the unique needs of the island communities. We thank you for your continued support of the insular areas as you are considering OIA's 2008 budget request.

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Mrs. CHRISTENSEN. Thank you for your testimony, Mr. Cohen.  
I recognize myself for 5 minutes.

Mr. Cohen, I am interested in reviewing what you describe as the new competitive allocation system for the CIP dollars. Can you tell us how you determine the base amounts for each Territory and review the competitive criteria for us?

Mr. COHEN. Sure.

First of all, the base amounts were established largely out of historical practice, so we wanted to establish baselines that did not significantly alter the levels of funding that we have been provided historically. And as you know, typically, since the economies of American Samoa and the Northern Mariana Islands were less developed, especially in terms of critical infrastructure, than Guam and the U.S.V.I.—even though, obviously, Guam and the U.S.V.I. also have very severe infrastructure challenges—we continued a higher level of funding for the baseline for American Samoa and the CNMI than for the other two.

The criteria were designed to encourage the insular areas to improve their financial management practices, and in our budget, as I outlined in my testimony, we have limited areas of flexibility; and we sought to develop an area where we can provide incentives for improving fiscal management. And that is what we sought to do, but we wanted to limit this so that, as Governor Togiola has suggested, we did not create wild swings in funding from year to year. So we established a range from the baseline, up to \$2 million above and up to \$2 million below, where the ultimate allocation might fall on the basis of how each of the Territories in this case performed in the competitive criteria.

We have a set of 10 criteria. I could go through them if you would like—you know, we can submit them for the record—but they are all designed to improve fiscal management, including timeliness on single audits, responsiveness to inquiries and questions that are raised in Inspector General reports, GAO reports, things of that sort.

Mrs. CHRISTENSEN. Can I ask you, what were the specific performance criteria that led the Virgin Islands to be penalized to the extent of a reduction in their CIP funding over their baseline?

Mr. COHEN. Sure. And we would not characterize it as being penalized because, I guess, the way the allocation works is, you know, an insular area might improve financial management from one year to the next, but if all of the other Territories make greater improvements as determined according to the 10 criteria, then that insular area may still end up with less of an allocation. But in the case of the Virgin Islands, as I recall, the number one factor was the failure to be timely on the single audits.

The other three Territories—Guam, the U.S.V.I. and American Samoa—are all current on their single audits; and we believe the U.S. Virgin Islands is one single audit behind. So, on that factor, which we attach a lot of importance to, the U.S. Virgin Islands, even though it has made very commendable progress in recent years in catching up on its single audits, was still behind the other three Territories.

Mrs. CHRISTENSEN. Thank you, and you know—let's see. We have talked about the decreasing of our allocation over the last couple of years, but you know that our islands remain under Federal court orders with the Department of Justice and EPA, which estimate that it will cost about \$50 million to construct new wastewater treatment plants to comply with the Clean Water Act.

I can support your efforts on the compliance of the single audit and the other criteria, but I am inclined to believe that an additional criterion relating to complying with court orders or consent decrees might be needed to really address the significant cost that such compliance actions will have on the already-strained budgets of insular governments.

So what is your view on the impact of court orders and consent decrees on CIP funding? Do you think that it should be another criterion that would be considered?

Mr. COHEN. Thank you for the question, Madam Chairwoman.

That certainly could be considered, and we have thought about it. Our thinking to date has been that the state of infrastructure at each of the insular areas is—well, they are all facing such great challenges that it is very hard to distinguish between them in terms of consent decrees and court orders, not to say that it is not relevant; and we are certainly open to taking another look at that because it is certainly—you know, it is certainly a very valid point.

But I believe there are consent decrees active in all of the Territories, with the possible exception of American Samoa where there are also similar needs. I mean, we funded the hospital with a certain allocation, not because it was under consent decree, but it was in violation of certain other standards that might have affected its eligibility for other Federal funds.

So, between consent decrees and situations such as those faced by LBJ Medical Center, all of the Territories have those issues. But we have been thinking about this, and as of course you know, we received an additional source of funding specifically for water and wastewater projects recently, and we established criteria, competitive criteria, again for all of the Territories to be able to apply for this fund, for this amount of funds. It is just under \$1 million, and we do include consent decrees in that. In fact, the criteria are whether the Territory is subject to a consent decree and, if so, whether the proposed activity will directly assist in meeting

consent decree deadlines and obligations. And we have three other criteria, particularly because these additional funds, I think, are more focused on helping the Territories get out from under consent decrees and comply with their requirements.

Mrs. CHRISTENSEN. Are those funds competitive also?

Mr. COHEN. They are competitive. In fact, I think, for Fiscal Year 2007, the entire amount, which is \$990,000, is going to be provided to the U.S. Virgin Islands for wastewater system infrastructure and improvements. I think mostly the sewer system on St. Croix is mandated by the USEPA because we know that there are very urgent challenges both on the ground and legally that are being faced by the U.S.V.I. now.

Mrs. CHRISTENSEN. OK. Beginning in Fiscal Year 2005, Congress and Appropriations gave the Secretary the authority to modify the covenant CIP funding formula to address appropriately court-ordered infrastructure projects. It sounds as if everything else was equal, that that would also be a criterion, if I understand your response.

Mr. COHEN. Yes, definitely. We have it as an express criterion for the water and wastewater funds, and are very open to considering your request that it be an express criterion for the CIP funds as well. I mean, that is certainly a reasonable thought; and you know, I guess I would welcome the opportunity to continue the dialogue with yourself and your staff and the staff of the other members of the committee on this issue.

Mrs. CHRISTENSEN. Thank you.

I now recognize Congressman Fortuño for questions.

Mr. FORTUÑO. Thank you, Madam Chairwoman, and again, thank you, Assistant Secretary Cohen, for making the effort to be here with us this morning. We truly appreciate the effort.

I will go back to my line of questioning with the Governors regarding the Territories' economy. Certainly, actually, you mentioned that your office is trying to attain self-sufficiency for the Territories. I would like to discuss this further.

Can you identify—or certainly you have provided particular assistance to the Territories to identify their comparative advantages, and you discuss or identify some of those advantages, at least pertaining to two Territories that represent the respected Governors here this morning; and second, as to those industries that perhaps may have the most potential, given the actual present circumstances, they are very different. Certainly, we heard, for example, of how different the two economies may be even though there are similarities in their political status right now.

So can you expound on this, please?

Mr. COHEN. Sure. Thank you very much for the question, and they are very different circumstances.

Guam, of course, is going to be the recipient of approximately \$14 billion of investment from the Department of Defense not only for the relocation of the III Marine Expeditionary unit from Okinawa to Guam, but also complementary upgrades that are going to be occurring at Anderson Air Force Base and the naval base in Guam. So that amount of money going to the economy, is going to fund a lot of construction, and the percentages that Governor Camacho has cited as to contribution—30 percent military,

60 percent tourism—will perhaps alter somewhat with this type of infusion of funds into the economy.

They continue to have a very strong tourism sector primarily from Japan, but they are looking at opportunities to diversify outside of that, as well; and I know Governor Camacho has been very active in looking at other opportunities of maybe using Guam as a Customs clearing center where goods can be transferred, you know, where Customs could clear goods there, and they can be shipped on to the U.S. mainland.

There has been investigation of whether Guam could serve as a good financial services center or banking center for that part of the world because one of the competitive advantages that all of the Territories share is the protection of the U.S. flag and the U.S. legal system. So Guam, which refers to itself as America in Asia, can provide that type of safety and security, maybe for a trust fund business or other types of financial services in that region of the world, bringing the U.S. legal system there.

So there are a number of opportunities that Guam has been looking at.

In American Samoa, it is a very different circumstance. You know, Guam is a transportation hub for Asia and Micronesia, and it benefits from that. American Samoa, as Governor Togiola pointed out, is very isolated both geographically and in terms of the air service that it desperately relies upon.

Its competitive advantages include the benefits of the U.S. flag; it has more flexibility with respect to wages because of the special industry committee structure that Puerto Rico once used and American Samoa still does. As the Governor has suggested, they are looking at the contact center industry; in other words, you know, taking advantage of what the different cost structure businesses might encounter there.

Plus, the fact that the workforce is fluent in the English language and it is a different time zone, people in American Samoa can work while people in England are asleep and vice versa, and that might make some sense, but that would require an investment in a fiberoptic cable, which is something that the Governor has put into his budget request. And we have honored that in our budget request, so that is a possibility.

American Samoa, like Guam, is physically a very beautiful place, and in fact, American Samoa is, if I may say so, more unspoiled, less developed and offers a great deal of opportunity in tourism. As the Governor suggested, the tourism industry is not that well developed yet, which means that there is a lot of room to grow if we can solve the transportation problem, especially ecotourism.

American Samoa, I think alone with Puerto Rico, has a national park that is in a tropical rainforest environment. So that is unique to American Samoa and Puerto Rico. And, you know, it is a beautiful place; the outer islands of Manu'a, these are spectacularly beautiful places. If we can get people out there, it will be very popular, but solving the transportation issue is the key.

Mr. FORTUÑO. Thank you again.

Thank you, Madam Chairwoman.

Mrs. CHRISTENSEN. The Chair now recognizes Ms. Bordallo for questions.

Ms. BORDALLO. Thank you. Thank you very much, Madam Chairman.

I was listening very carefully to Mr. Cohen's comments about the islands. As island representatives, of course, we always feel they are equally as beautiful.

Mr. Cohen, I note that the Fiscal Year 2008 budget request represents the fourth consecutive year of proposed capital improvement grant funding under the new criteria. The baseline for both Guam and the Virgin Islands is reportedly \$3.36 million. Yet, I believe that Guam, if you average the level of funding provided under the program for the past 3 years, has come out below this baseline.

Can you please comment on how effective you believe the established competitive criterion has been toward improving financial management practices in the Territories; and in addition to that, have you shared the CIP competitive criterion with the territorial Governors and public auditors?

How transparent is the process? Do they receive a scorecard each year?

After your comments, if the Governors would like to respond, please do.

Mr. COHEN. Thank you very much for the question, Congresswoman Bordallo.

First of all, I think the system has been effective. For example, you mentioned that, as for Guam, the average funding in these past years is below Guam's baseline. Well, in Guam's first year, it scored fairly low, and Governor Camacho is fairly new; and obviously you inherit a bureaucracy, and it takes a while to identify areas that can use improvement. He immediately came to us and said, I want to know why we scored the way we did, what we need to do to score better and—as we would offer to the governments of all of the insular areas, which by the way, are equally beautiful. If I was not clear on that, I want to make sure that is on the record.

Ms. BORDALLO. Thank you.

Mr. COHEN. We honored his request, and we sent the head of our Budget and Grants Management Division out to consult with them and the relevant members of his team; and the next year, their score improved dramatically.

So what we are trying to do is send the right signals. It is never going to be an exact science, but we want to send the right signals. We want to make it very clear that good financial management practices will be rewarded and that the converse is also true. We have been under tremendous pressure from the GAO reports and the Inspector General reports, and rightfully so, to send stronger signals to the governments of the insular areas that financial management practices, especially with respect to the Federal funds, are of utmost priority.

The criteria, themselves, have been shared. They are transparent, and I think we can investigate ways to—and we are happy to share the results of the scoring practice. I mean, we have sort of—I mean, this is a newly conceived and a newly developed program, and we are very much open to suggestions. I believe—you know, we do not put these on our Web site, but we do not want to make any of our Territories feel that we are making them look

bad or favoring one over the other; we are very happy to share this process and be very transparent about it. I mean, that is our obligation in any appropriate way that does not make it look like we are being overly critical of any of the Territories.

So we are open to suggestions on how to do that, and we are free to share the results of our analysis.

Ms. BORDALLO. Just on that same note, Governors, are you satisfied with this new practice?

Governor TOGIOLA. I think the record should show that when this program was—when this was first announced, I was one of the most critical ones that resisted handling the CIPs this way, and more so after the first 2 years when we lost funding because of the grading. We decided to stop wondering what they are doing with it and just go ahead and do it; and since then, they have improved my score, and I have been happy, so—

Ms. BORDALLO. Very good, Governor.

Governor Camacho.

Governor CAMACHO. Definitely, what David had expressed is exactly what happened. Recognizing that Guam was below the baseline and it scored poorly in the previous years, what could we do to improve it? With their guidance, we have improved and have benefited from it.

I think one of the things we are requesting, for example, now, is some help on the new gantry crane, but as I mentioned earlier in response to your inquiry, with the financial management improvement plans that have been there in a single audit, we went from 11 qualifications, I think down to one or two now. So there have been tremendous improvements in our reporting requirements, and it has, as you mentioned, resulted in not only better scores, but we have been rewarded.

Ms. BORDALLO. Very good, and I am happy. I am always out for new ideas and new methods, and if it is working, great.

Now, one other question. Has the criterion been modified at all since the implementation?

Mr. COHEN. Yes. Yes, it has.

When we originally developed the criterion, we focused not only on good fiscal management but also on providing a good slate of projects; but we subsequently determined that the slate of projects kind of takes care of itself because we have a planning process and we have the ability to say that the slate of projects you presented is not consistent with your plan. We communicate back and forth with the island governments, and we really wanted to send a strong, clear, unambiguous signal that fiscal management needs to be improved in the Territories, in all of the Territories.

It needs to be improved in all of the States; we do not want to single out the Territories, but we want to send a very clear, unambiguous signal that this is our priority.

And the quality of the projects is also very important, but we have other ways to address that.

Ms. BORDALLO. Madam Chair, I have one simple, little question here for Mr. Cohen again.

This has to do with the \$30 million compact impact funding. It is allocated based on a census of the FAS citizens.



What are your plans for the upcoming census and how will this be conducted?

Mr. COHEN. Well, we are planning, again, to work with the island governments to help on these enumerations and to make sure that our methodology is standard across all of the island jurisdictions and that there should not be any sort of undercount or overcount bias of—

Ms. BORDALLO. Inflated numbers, right?

Mr. COHEN. Right, and as you know, we are required to do this no less frequently than every 5 years—

Ms. BORDALLO. Five years.

Mr. COHEN.—and I guess we are coming up on the next one soon. But we have a budget for this.

The budget actually comes out of the \$30 million. The first time we did it, we offered from the Office of Insular Affairs to fund that out of our technical assistance grant, but for all subsequent years, we will take that out of the \$30 million. It is not going to be a significant deduction from the \$30 million at all, and it is an investment to make sure we are counting accurately; but of course, that is a very important procedure because it determines for up to the next 5 years how much compact impact money each of the jurisdictions is going to receive.

Ms. BORDALLO. Yes.

Governor Camacho.

Governor CAMACHO. Thank you for allowing me to just comment on this.

I wanted to commend OIA and David Cohen and his staff for having an open mind when it comes to the expenditure of compact impact moneys. What we did was a very unique thing in leveraging the moneys. We were taking \$6.1 million out of our allotment, and by entering into a municipal lease over 20 years, we are now able to build for schools—

Ms. BORDALLO. Yes.

Governor CAMACHO.—worth millions of dollars that, if we had just outright spent, we could not have done it.

So finding ways to take the limited funds we have and leveraging them over the years has allowed us some brick-and-mortar projects that would be there for quite awhile.

So I just wanted to commend them for having an open mind and allowing that to happen.

Ms. BORDALLO. Thank you.

Thank you very much, Madam Chair.

Mrs. CHRISTENSEN. Thank you.

Mr. Cohen—let's see. I have a few more questions.

You know, we have benefited, as have all of the other Territories, from the outreach to investors and to the economic conferences that have been held; but I am curious to know if any thought has been given to also putting some focus on the development of small businesses, small local businesses, either on their own or in conjunction with some of these new investors that are coming in.

Mr. COHEN. Thank you, Madam Chairwoman, for the question.

Yes, we give a lot of thought to that, and we give a lot of priority to it. Our ideal scenario is not that a big company will come in from off-island and establish a presence in the islands and compete

out all of the local businesses. In fact, that is the type of thing we are trying to avoid.

We are very much focused on what we call “win-win opportunities.” I mean it is a slogan, but it is also something that we try to put substance to and take very seriously, and that is facilitating strategic partnerships between local small businesses on the islands and off-island businesses so that both can prosper.

I mean, the typical scenario is, you might have a small business on an island that does not have sufficient capital or technological expertise or business expertise or marketing channels to take its business to the next level, that can partner up with an off-island company that provides that so that both can prosper. The off-island business can take advantage of the local knowledge and presence of the small business on the island, and the small business on the island can benefit from the additional capital expertise and all of that. So that is our ideal scenario.

A lot of the success stories that we have had have been ones where island businesses themselves have benefited. There have been IT entrepreneurs, for example, in American Samoa that have teamed up with other island businesses to provide services in different island communities; and for us, those are the most exciting opportunities.

Mrs. CHRISTENSEN. Well, we see the emphasis on the investment coming in, which is, again, very important. You know, we would like to see a little more. I am sure the Congresswoman and my Ranking Member would also appreciate the help for some of the small, struggling, locally owned businesses in the Territory as well.

A similar question that I have.

You heard Governor Camacho talk about the impact of the military buildup, and even bringing these wealthy investors into the Territory has a tremendous social impact on the Territories. Has OIA given any consideration to looking at not only the economic benefits and the infrastructure needs for bringing in these businesses, but how we can ameliorate some of the, perhaps even negative impacts that the residents, the longtime residents, of the Territories might experience?

Mr. COHEN. That is a very good and important question; and of course, I am familiar with the situation, particularly in the U.S. Virgin Islands, where incentive programs actually had a lot of high-wealth individuals relocating and moving their homes to the U.S. Virgin Islands.

And, of course, as you know better than anyone, it created a lot of good, and it also raised certain issues as to interaction between the folks who have been there for a long time and folks who are new to the community. That is something—

Mrs. CHRISTENSEN. Property values, to name one impact?

Mr. COHEN. Sure, and it goes back and forth.

Property values can have the effect of pricing middle-class people out of the market, but yet more jobs are provided by the demand for these types of homes. So you are right. There are positive and negative impacts.

We are open to using our technical assistance funds to study these impacts when appropriate. We certainly like to keep them in mind. I mean, our office is, I guess in the Federal executive branch,

the one that is most aware of the cultural sensitivities of all of the island communities in the Pacific and the Caribbean more than any other Federal executive branch office. We keep that in mind when we do our business opportunities missions and our conferences, but we can certainly do more to address those issues.

Mrs. CHRISTENSEN. OK. Let me try to get in one other question here.

In the budget request, you make mention of the Island Fellows Program which you offer to several different universities, and I notice they are all Ivy League universities. So I have two questions, really.

One, do you seek out students from the Territories when you do this? Do you look at HBCUs and other minority-serving institutions? Do you look for fellows at the University of Guam or at the University of the Virgin Islands to help our young people develop these skills and to help give them an opportunity to help their communities?

Then, how is the final product from these students used? Are there private-sector assessments made available to the island governments? Are they provided to Congress?

Mr. COHEN. Thank you very much for the question. And I think in the question, there was, I guess, a suggestion that we do reach out to other schools.

Mrs. CHRISTENSEN. Yes, in all of my questions.

Mr. COHEN. Yes. Well, I think it is an excellent suggestion, but let me give you an idea of how we sort of got to this point with the Island Fellows Program. To skip ahead to the end, I think your suggestion is an excellent one, and we will definitely look at that.

The Island Fellows Program started as, really, just a joint program with the Wharton School, the University of Pennsylvania. Actually, it started from an offhand suggestion that Secretary Norton, at the time—you know, my former boss at Interior—said:

“Well, can’t we send bright, young business students from Harvard Business School out to the islands to help think through some of these economic issues?”

I am actually a graduate of the Wharton School, and I said, “Well, Harvard. We can do better than that.” so I went to Wharton to establish the program there.

The first year was very successful, but after that, it was suggested that—well, we expanded out, and we have expanded it beyond just Ivy League schools.

I just got back from a trip to Wharton and Harvard to recruit up there, but we also have students—we have had students from the University of Hawaii. We have had many students from there. We have had students from the University of Virginia, Northwestern University, George Washington, Georgetown, and we are always looking to expand it out.

I think your suggestion to expand it out maybe to the University of Guam—well, one issue there is, we have traditionally used MBA candidates because of the nature of the program, so some of these colleges do not have MBA programs. But we can still think that through.

We are looking for ways to bring folks from the islands into our office either as permanent employees or for the summer, and we

have a very good record of having done that, but we certainly would be open to doing that.

Part of the charm—or one of the greatest benefits, I would say, of the Island Fellows Program is, even though we have hired students who are from the islands—we have had folks from Palau, and some were just from, like, Hawaii. But one of the most satisfying things from my perspective is that most of the folks that we have hired have no background in the islands, but as a result of their experience, they form what I hope will be life-long affinities with the islands; and often these folks go on to careers in high-powered consulting firms or investment banks or whatnot, but yet they are always friends of the islands.

I mean, we have folks coming back from a few-weeks' stay in the islands, and then they start referring to the community they visited as “we,” you know, like “we” have to improve our economy, and that really struck me. So I like the idea of bringing folks who have never been exposed to the islands out to the islands and creating life-long friendships.

But we have also benefited from the perspectives of those who are from the islands, and it creates good interaction. So I consider that an excellent suggestion which we will definitely look into.

Mrs. CHRISTENSEN. Thanks.

Mr. Fortuño.

Mr. FORTUÑO. Yes. Thank you again, Madam Chairwoman.

Mr. Cohen, if we may follow the economic development issues, actually, in our earlier discussions with the Governors here, we were acknowledging the fact that the tax incentives that were in place for so many years are gone, and actually, I made some comments after reading the report, the report that came out of Congress, essentially stating that in terms of future, long-term economic policy, it should be non-tax-based and what have you.

Have you thought of what kind of incentives, economic and otherwise, may be needed to promote greater private-sector investment and development in the islands?

Mr. COHEN. Yes, we have given a lot of thought to that. I want to be careful in not suggesting an administration position on any particular approach, because we are still in the process of working that through; but if you look at the tools that are available, arguably they are fairly limited. You have tax incentives, and we have worked with those, and we have experienced some problems and also some successes. We have trade.

Now, arguably, the ability to use trade incentives is being eroded with the very positive development of expanding free trade around the globe, and the more foreign nations that get, for example, duty-free access to the U.S. or other sorts of favored access to the U.S. market, the less room for maneuver you have to provide those benefits to the Territories in a way that creates a real competitive advantage. So, arguably, the value of trade incentives is going down.

Then you have direct grant assistance, and we have been working to sort of reduce the Territories' dependence on direct grant assistance. There are other things, like helping to build up the infrastructure, and we are doing that as much as we can.

As Governor Camacho pointed out, we are also looking at ways to be creative with the grant assistance we have, so that it can be

leveraged and that the private sector and other financing sources can come in and really carry most of the burden.

Mr. FORTUÑO. Mr. Cohen, if I may—and I am sorry to interject here—there is a reason why I called this structure, political structure, 18th century solutions to 21st century realities; and everywhere I turn, I think we are facing the same challenges in that the world is changing for the better in terms of opening up markets, that actually we have WTO restrictions as to what can and cannot be done. So that creates additional burdens on our economic development possibilities; and we are turning back to the same problems, actually, that we have been facing.

And actually, if I may say so—actually, Governor Tulafono mentioned only two plans that were created or built in X number of years given all these tax incentives; and I am very concerned. Really, we have a responsibility here. There is a political aspect to this, but certainly I have a feeling that we are getting to the same point over and over again.

There is only so much we can do short of a major influx of new money for military construction that will be occurring in Guam, for example. Are you in agreement with this?

Mr. COHEN. Well, I want to be careful to say, that is really the only tool we have, but I certainly accept your assertion that the tools we have are limited. That is one of the reasons that we have put such emphasis on trying to bring the private sector into this, because at the end of the day, the Territories are going to be strong if they are strong economically, and they can only be strong economically if they have the strong private-sector-driven economies.

We are talking about, well, how do you finance all the infrastructure, how do you finance the health care needs, the education needs?

Well, jurisdictions that generate sufficient tax revenue to provide for all of these needs do not have to worry. It is jurisdictions that have private sectors that are too small and are too thin and concentrated, lacking economic diversification, so that they cannot reliably generate the revenues they need to provide the critical needs.

Well, those are the ones that are in trouble. Those are the ones that need to keep turning to the Federal Government.

Now, the island communities, as you well know, start with so many disadvantages in terms of remoteness, resource poverty, a small population base. Puerto Rico less than the other insular areas, but these are problems throughout the island communities; and the Federal Government cannot solve these problems on its own and the island governments cannot solve these problems on their own. It really all comes down to whether there is a strong, healthy, private-sector-led economy that we can establish in the islands. There are barriers to our ability to do this.

But there are competitive advantages that the island communities have. We have to stress those, enhance those, make sure everybody knows about them, do our best to promote the islands, because ultimately that is really the only way that the islands are going to have long-term fiscal and economic health.

Mr. FORTUÑO. Thank you again, and I couldn't agree with you more. Thank you again, Madam Chairman.

Mrs. CHRISTENSEN. Thank you. Ms. Bordallo?

Ms. BORDALLO. Thank you again, Madam Chairman. I have one question for Mr. Cohen. Could you expand on what efforts are currently being undertaken by OIA to address high risk grantee status of some territorial government agencies with certain Federal Government agencies, including the Department of Education, for example? Is OIA taking a lead role in coordinating with other agencies in this area? This is the reconciliation of Section 30 funds owed to the government of Guam, say, by certain Federal agencies. It remains an ongoing challenge, and I have been asked over and over by our local senators. I just returned from Guam yesterday, and the Governor and I were referencing this earlier. Certain fees and withholding taxes collected are not always covered over to the Guam Treasury by individual and relevant agencies. Can you give us some idea about this? What is being done to improve this?

Mr. COHEN. Sure. Thank you, Madam Congresswoman. We put a very high priority in making sure that the Territories get their due, what they are entitled to under Federal law. So my staff has been very active in trying to make sure that, you know, these Section 30 amounts are properly accounted for and that the government of Guam in particular, of course, in this case gets what it is entitled to. Our chief budget officer, Charlene Leizear, actually takes very—has been very actively involved. We also participate in the All Island Tax Association meeting annually with the IRS where we work through these issues. Because a lot of this is under the control of other agencies, you know, we certainly are very active behind the scenes just to make sure that they are engaged, and especially in recent years we have a lot of good cooperation from the IRS. But we also recognize that because of upswings and downswings in sort of the accounting as to what is ultimately owed under Section 30, that it can create a hardship on the government of Guam. So what one thing we are able to control is to the extent that say a large amount is owed because of, you know, a perceived overcompensation on the Section 30 funds, we have been giving Guam more time to repay, that they wouldn't have to, you know, pay a larger amount up at once, but the IRS has been catching up on its process of determining how much—of making sure Guam is paid everything it is owed, including from back years, and then we have provided greater flexibility to the government of Guam, recognizing the Section 30 amounts will likely increase as this process continues to not have to pay back all at once. We have given them 3 years to pay back an amount that hopefully will never have to be fully paid back because Section 30 amounts Guam is entitled to will be increased.

Ms. BORDALLO. Governor Camacho, is there any area that you wish to bring up at this point in regards to this?

Governor CAMACHO. As mentioned earlier, we had a director here I believe that worked with you in OPM. And I think those matters are being resolved. And we are grateful also to the fact that where years the government overestimated Section 30 we are allowed a number of years, over 3 years to pay it back, settle. So we are very much appreciative of that.

Ms. BORDALLO. The other part of that question, any efforts at OIA to address high-risk grantee status of the Territories?

Mr. COHEN. Yes, Congresswoman. We have been funding a number of programs to help give the insular area governments the tools they need to address these fiscal management challenges, and other agencies have put either entire—well, you know, we had a high risk situation with the government of American Samoa, and other agencies have put various agencies, various local agencies in Guam, U.S. Virgin Islands and other communities in high risk status, and we recognize that it is often a matter of capacity. It is very much a matter of capacity. So we have put a lot of resources and a lot of effort into capacity building for fiscal management. We have a strong partnership with the USDA grad school. We have a program funded to the tune of about \$2 million every year where they provide intensive training to fiscal managers in the islands. We host annual conferences where training occurs, and it is always attended at a high level by the Office of Insular Affairs. We have provided funds for hardware, software, fiscal hardware and software. As Governor Camacho has pointed out, we have funded the fiscal management improvement plans for a number of agencies in Guam, Department of the Administration, Department of Education, as you have suggested. We have recognized it is a resource issue. We also recognize that the island communities have very serious challenges that they have to face, you know, to have good fiscal management. They have smaller population bases, you know, it is harder to attract talent to the islands. Basically, the pay scale is lower than what you get in the States. So you don't have enough of a home grown talent pool to rely on. You know, you can't pull folks in from neighboring counties or neighboring states because you are in the middle of the ocean. And to attract, you know, off-island talent, you generally have to—and keep it there, you have to pay beyond what your typical pay scale is. So we recognize there are inherent difficulties—not to make excuses. We recognize there are challenges that simply are not faced in mainland communities so we devote resources to try to overcome those.

Ms. BORDALLO. Thank you. Thank you, Mr. Cohen. Madam Chairman, I have no further questions, but I do want to make a comment. We are actually witnessing a historic meeting today. I think after 12 years we have re-established the Insular Affairs Subcommittee, and by re-establishing this committee I think it brings specific attention to all matters pertaining to the Territories, and I am extremely pleased with that. It gives us a unique advantage, and Madam Chairman, I am very pleased to be a part of this re-establishment of the Insular Subcommittee, and I want to thank the Governor from American Samoa, the Governor from Guam and of course you, Mr. David Cohen, for being a part of this historic meeting. Thank you.

Mrs. CHRISTENSEN. Thank you. Mr. Fortuño also—he will return shortly, but he doesn't have any further questions. Of course I have one more.

Mr. Cohen, when they appeared before the full committee 2 weeks ago, as you heard me say in a question to Governor Camacho, both the Inspector General of the Department of Interior and the GAO representative endorsed the idea of a chief financial officer as a good idea for the Virgin Islands and perhaps the other islands. So in light of those recent GAO reports on the severe

problems in financial management in the Territories as well as the reports from the Inspector General, do you still oppose a CFO or similar officer in the USVI? And if so, why?

Mr. COHEN. Madam Chairwoman, we are happy to take another look at it. You know, the last time the bill came up, you know, to be frank, we were put in an awkward position because there was, you know, obviously, you know, you had a position that was well reasoned and as reflected in your legislation, and the Governor had a different position. And in those situations, we don't choose between oh, well, we would—you know, side with the Congresswoman over the Governor or the Governor over the Congresswoman. In situations like that, you know, we would typically want to defer to the institution where there is the—where the people of the Virgin Islands would have the most say. So that is why, you know, we would—you know, our—

Mrs. CHRISTENSEN. I agree it was a difficult position.

Mr. COHEN. Yeah. But what I would want to say—and that is because there is a split. So when in doubt, regardless of the personalities or whatever, you know, we would tend to favor, you know, deferring the solution to the institution where local people have the most say, and of course you are elected by all of the people of the Virgin Islands, but you are serving a body where you are the only voice from the Virgin Islands as opposed to, you know, a local legislature that is fully elected by the people of the Virgin Islands. So that has nothing to do with the merits of the proposal. That was just sort of the institutional difficulty we were placed in.

Mrs. CHRISTENSEN. But you could probably see it, I mean, God willing this will never happen, but there could have come a time where the situation was so dire that it might have required that you not defer to the local legislature but do what was the right thing to do in the interest of the people of the Territory.

Mr. COHEN. Oh, absolutely. Absolutely. And, you know, our first preference is when there is a disagreement on substance between elected officials is to, you know, try to defer to one institution or the other based on local control. But I will say if, for example, you know, with the new Governor in the U.S. Virgin Islands, you know, if the government there were to support a proposal that you were to put forward, we wouldn't be put in that situation. I couldn't guarantee any particular result without having cleared it through the administration.

Mrs. CHRISTENSEN. Sure.

Mr. COHEN. But it is a different—put aside the substance, that puts us in a different situation as to what institutions we would tend to defer to.

Mrs. CHRISTENSEN. Would you ever remain neutral if it was a good—if there was a division between different offices in a Territory and—but a good proposal?

Mr. COHEN. I am sorry. Could you say that again?

Mrs. CHRISTENSEN. Would you ever consider remaining neutral, not having an opinion?

Mr. COHEN. Yeah. We would take every situation as it arises. We do have a preference to allow local decisions to be made locally, and again, that has nothing to do with the substance. And you are right, the substance—the facts on the ground could reach a point



where we would override that preference and say, you know, there is a compelling need to, you know, impose a Federal solution because a local solution, you know, may result in, you know, irreparable harm or something of that sort. So the bottom line though is that we are happy to take another look at whatever proposal you have, and we are happy to work with you on that, and of course we will be in contact with your office, and the Office of the new Governor and especially if there is agreement between your two offices, that is a completely different situation for us.

Mrs. CHRISTENSEN. OK. If there are no further questions, I move to have the testimonies of the U.S. Virgin Islands Governor John deJongh and the Commonwealth of the Northern Mariana Islands Representative Pete Tenorio entered into the hearing record, and without objection, so ordered.

[The prepared statement of Governor deJongh follows:]

**Statement of The Honorable John deJongh, Jr.,  
Governor of the U.S. Virgin Islands**

Madame Chairwoman, and distinguished members of the House Subcommittee on Insular Affairs, it is an honor for me to present testimony today on the state of the Virgin Islands and on some of the critical issues facing our Territory.

As you know, I was privileged to be elected by the people of the Virgin Islands last November as their governor. While our Territory has made undeniable progress since the days of appointed governors, we are still challenged by difficult, though not intractable, problems. Thirty-five percent of our children still live in poverty. Our family incomes are a third lower than the poorest State in the Union. As a group of small islands geographically removed from the United States mainland, our cost of living is significantly higher than the average American community. Our economy is overly dependent upon tourism and requires further diversification. Like many of our border states, our social services and the fabric of our community are strained by illegal immigration and drug smuggling. And while the fiscal condition of our government has improved in recent years, much more remains to be done to close the gap between the standard of living in the Territory and that on the mainland.

It is my fervent belief that the people of the Virgin Islands have the capacity, the strength, and the will to successfully address these challenges over the next four years. As I have said at home, the State of our Territory in the midst of these challenges is one of hope and great expectations. And while I will call on our proud and resilient people to unleash their imaginations, their ideas and their energy to help my administration build a better future for all, there are also issues where the Federal Government—including this Congress—must play their part as well. It is in these areas that I would like to focus my remarks today.

**Property Tax Reform**

Economic growth and development in recent years has helped generate the marked improvement in the Government's financial condition, but it has also come with social costs that cannot be ignored. In particular, growth and development invariably bring rapidly increasing property values which, if not addressed, can threaten to tax homeownership out of reach for the average Virgin Islander. The ability of the Territorial government to deal with this problem has, as you know, been hampered by a recent federal court decision reviving a colonial-era statute which severely limits the authority of the Virgin Islands Government to administer its real property tax system.

Under this outdated statute—enacted by Congress in 1936 and previously thought to have been repealed by the 1954 Revised Organic Act—the Virgin Islands Government is prevented from exercising the authority enjoyed by States and local governments on the mainland to tax real property on the basis of use or other rational classification. By requiring, for example, a uniform rate of tax for both residential and commercial property, the 1936 statute puts at risk long-standing Government policies designed to develop the economy, promote social welfare, and protect homeownership in the Territory, including capping residential assessments during any assessment period.

Without the authority to limit property tax increases caused by rising property values—through capping assessments or phasing in increases—the revived 1936

statute may quickly put land and homeownership beyond the reach of many Virgin Islanders. This is particularly true in St. John, where development has resulted in significant increases in property values in recent years. The 1936 statute also puts into legal question other Government policies designed to promote economic and social development, including taxing agricultural land at lower rates than commercial land and providing veterans preferences.

I want to thank you, Madame Chairwoman, for your leadership in sponsoring legislation to repeal this anachronistic law and to clarify that the Virgin Islands has the same powers and authority as any other American jurisdiction to determine and to administer its own property tax system. I am pleased that the House moved quickly, upon the convening of the 110th Congress, to pass this important and necessary legislation. I am hopeful that the Senate will act quickly as well so that the legislation can be signed into law as soon as possible.

#### **Control of Our Borders**

Madame Chairwoman, I would also like to commend you for your efforts to secure a Border Patrol Unit for the Virgin Islands. As you know, currently there is no Border Patrol station in the Territory, with the closest station responsible for protecting our borders and our coast line located in Puerto Rico. The problem is that the station in Puerto Rico must focus on the hundreds of miles of coastline in that part of the Caribbean, leaving the coastline and coastal waters of the Virgin Islands largely exposed and vulnerable to human smuggling and drug trafficking. As a result, international smugglers and organized crime have been increasingly utilizing our Islands as a major transshipment point into the United States. In addition to this implications for our national and regional security, the scourge of smuggling and illegal drug trafficking has a direct impact on the crime rate in the Territory and on our quality of life.

I am therefore pleased to reaffirm my commitment to work with you, other Congressional leaders and the Department of Homeland Security to establish a Border Patrol Unit in the Virgin Islands as soon as possible.

#### **Elimination of the Cap on Rum Excise Taxes Returned to the Virgin Islands**

Madame Chairwoman, I would also like to lend my support to your efforts to eliminate the "cap" on the amount of federal rum excise taxes that are returned to the Virgin Islands each year under the provisions of the Revised Organic Act and the U.S. Internal Revenue Code. As you know, Congress is required periodically to extend the current formula for calculating the rum tax payment to the Virgin Islands. In the absence of such periodic extensions, the formula would be reduced, costing the Virgin Islands Government millions of dollars and putting at risk the Government's bonds which are secured by such tax revenues.

But even the temporary extensions, while welcome, cause problems for the local Government which could be eliminated by removing the cap entirely and allowing the Territory to receive the full amount of the federal tax imposed on Virgin Islands rum. First, the temporary extensions authorize the return of \$13.25 per proof gallon of rum produced in the Virgin Islands and shipped to the United States, while the full tax imposed by the Federal Government on Virgin Islands rum is \$13.50 per proof gallon. Under the temporary formula, 25 cents on each proof gallon of Virgin Islands rum is retained by the U.S. Treasury. Second, it is difficult to securitize long-term bonds with revenue streams that may be interrupted by unscheduled or unforeseen delays by Congress in extending the present formula. Indeed, the history of the most recent extension by Congress reinforces this point. Congress passed the last extension this past December—eleven months after the previous extension expired. While Congress made the extension retroactive and the Territory did not lose funds as a result, it nonetheless created concerns for the nation's financial institutions that hold our bonds and has the potential to affect both our bond ratings and bond capacity.

It is generally accepted that there are no policy reasons that stand in the way of Congressional action to remove the cap and allow the Territory to receive the full amount of the tax imposed on Virgin Islands rum. The tax was imposed, in the first place, not to raise revenues for the Federal government, but rather to ensure a commercial level playing field for domestically produced distilled spirits with which Virgin Islands rum competes in the U.S. market. Rather, it would appear that the reasons blocking a permanent solution to this problem up until now is a more practical one: under the Congressional budget rules, a Congressionally initiated legislative change must be "offset" with other revenues, but a permanent solution proposed by the administration as part of its annual budget proposals to the Congress does not. Accordingly, I would respectfully request that this Committee work with the House

Ways and Means Committee to urge the President to include a permanent solution to the rum tax formula in his next budget submission to the Congress.

#### **Elimination of the Discriminatory Cap on Medicaid Funding for the Virgin Islands**

Madame Chairwoman, as you are well aware, the ability of the Virgin Islands Government to assure adequate health care to Island residents is hampered by the discriminatory cap on Medicaid funds provided to the Virgin Islands and the other U.S. Territories. Medicaid is a federal-state program to provide for the health care needs of the poorest and neediest persons in our country. The quality of health care should not depend on whether an individual lives in California, Alaska or in a United States Territory. While, under your leadership, Congress approved last year an increase in the amount of Medicaid funds provided to the Virgin Islands, such increases only narrow the gap between the funds allocated to the Virgin Islands and funds the Virgin Islands would be entitled to if the Virgin Islands were treated as a State under the Medicaid formula. The Government of the Virgin Islands respectfully requests the Administration to support, through the IGIA process, further improvements in the Medicaid formula and to ensure that the neediest residents in the Territories receive no less favorable treatment than the neediest residents in the United States.

#### **Support for the Virgin Islands Economic Development Commission Program**

Finally, I would like to bring to this Committee's attention an issue which has profound implications for the fiscal and economic independence of the Virgin Islands. That issue is the unrestrained program of IRS audits which is having a significant adverse impact on our vital Economic Development Commission ("EDC") program.

As you know, residents of the Virgin Islands, as citizens of the United States, are required to pay Federal income tax like any other citizen living outside the United States. However, Section 932 of the Internal Revenue Code states that bona fide residents of the Virgin Islands are not required to file an income tax return with the IRS. They are required instead, to file their income tax return with, and pay the applicable tax to, the Government of the Virgin Islands.

The amount of the liability to the Virgin Islands, determined under the "mirror code" system, in most cases is exactly the same amount that they would otherwise have been required to pay to the Federal Government. The only exception is a provision under Section 934 of the Code which permits the Virgin Islands to provide economic development incentives through tax credits or tax rate reductions for income from sources in the Virgin Islands or income effectively connected with the conduct of a trade or business in the Virgin Islands.

Pursuant to this authority, the government of the Virgin Islands established, almost 50 years ago, an economic development program that was intended to diversify the local economy, create jobs for its citizens, and to lessen its dependence on the Federal Government. Under this program, the Virgin Islands government provided tax incentives to qualified businesses that established operations and invested in the Virgin Islands, and that met the program's criteria for creating jobs and economic opportunity for Virgin Islanders.

In response to concerns that some U.S. citizens claimed tax benefits who neither lived nor worked in the Territory, Congress two years ago tightened the income and residency rules as part of the American Jobs Creation Act of 2004 ("Jobs Act"). With respect to the rules for determining residency in the Virgin Islands, the Jobs Act replaced a "facts and circumstances test" similar to that previously used for determining the tax residency for aliens with a physical presence test, a closer connection test, and a tax home test.

At around the same time, the U.S. Internal Revenue Service ("IRS") initiated a comprehensive series of audits not only of individuals who participated in the Territory's EDC program, but also of many taxpayers who had moved to the Virgin Islands years earlier and who did not participate in the EDC program, as well as taxpayers who were born in the Virgin Islands but who had spent periods of their working life outside the Territory due to the lack of opportunities in the Virgin Islands.

Neither the Government of the Virgin Islands nor most responsible members of our EDC community have any objection to properly conducted IRS audits, performed in compliance with the statutes and rules governing such audits and with clear audit guidelines in place at the outset. However, it appears that the IRS has used the subjective nature of the pre-Jobs Act legal standard for determining bona fide V.I. residency as a license to challenge anyone who claimed EDC benefits as a

potential participant in an abusive tax shelter, rather than as a participant in a lawful economic development program duly authorized by the Congress.

Rather than facilitating and ensuring tax compliance and, if the facts warrant, ferreting out wrongdoers, the IRS audits have instead become a vehicle for undermining a Congressionally sanctioned and authorized economic development program through punitive and heavy-handed techniques, including repetitive, intrusive, and burdensome data and document requests. Unfortunately and unfairly, the IRS audit presumption seems to be that the taxpayer engaged in tax fraud unless he or she can prove otherwise.

The IRS tactics, however, go far beyond intrusive and burdensome data requests. In the course of these audits, the IRS has reversed its long-standing administrative practice and published position, and now claims that the statute of limitations never runs for V.I. taxpayers who reasonably and in good faith file their tax returns with, and pay their tax to, the Virgin Islands Bureau of Internal Revenue (BIR), as the law requires them to do.

In a General Counsel Advisory Memorandum published last summer, the IRS announced its new position that it has the right to audit the returns of a V.I. taxpayer as far back as they like and, if they determine under the subjective pre-Jobs Act test that the taxpayer was not a bona fide V.I. resident, that it can assess full tax and penalties even if the taxpayer has paid the correct amount to the Virgin Islands. Because the Virgin Islands statute of limitations will have run in many of these circumstances, the taxpayer will be precluded from seeking a refund of tax paid to the Virgin Islands, and thus be subject to double taxation. Moreover, since the IRS position reverses a previously issued IRS advisory memorandum and also runs counter to the general rule that persons can be audited for up to three years after filing a return, many taxpayers who are being audited no longer have the records to defend themselves.

Similarly, at least some IRS agents may now be taking the position that even a bona fide V.I. resident who underpays his tax to the Virgin Islands by even one dollar (even if this is a result of a good faith error) may now be subject to full taxation by the United States without regard to, or credit for, any payments made to the Virgin Islands. Such a position is not only not without legal support, but it operates perversely as a disincentive for our Bureau of Internal Revenue to audit and seek any underpayments of tax from our own taxpayers.

These heavy handed practices violate the due process rights of Virgin Islands taxpayers and have had a chilling impact on the Territory's EDC program, raising the specter of guaranteed and endless audits of virtually anyone who moves to, and invests in, the Virgin Islands. This is not, I would respectfully submit, what Congress had in mind when it enacted the Virgin Islands tax incentives at issue as part of the 1986 Tax Reform Act, or when Congress acted to include more objective factors in the determination of residency and sourcing of income as part of the Jobs Act in 2004. Without any consultation and indeed notice, these actions continue. On February 21, 2007, Treasury issued Notice 2007-19, covering statute of limitations that does not adequately address our concerns and has unilaterally imposed draconian measures on our residents. I hope that through my efforts, beginning with this testimony and continuing with meetings that had already been scheduled with both Houses of Congress and the Executive Branch, we will be able to restore a cooperative process going forward and that we will be able to revise, amend or replace these recent regulations and actions with policies and programs that work to assure our mutual goals.

I appreciate the efforts you have made along with other Members of Congress to rectify this wrong. Because this issue cuts at the heart of our efforts to diversify and grow our economy and to achieve fiscal independence, I would respect urge this Committee to support legislation affirming the previous federal policy that a tax return filed in the Virgin Islands shall be treated as a tax return filed in the United States for purposes of triggering the statute of limitations.

Thank you very much.

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[The prepared statement of Mr. Tenorio follows:]

**Statement of Pedro A. Tenorio, Resident Representative,  
Commonwealth of the Northern Mariana Islands**

Madame Chairwoman, members of the Committee, thank you for this opportunity to submit testimony today on the FY 2008 proposed budget for the Office of Insular Affairs. I apologize for being unable to be with you in person today. I am in the Commonwealth accompanying Senate Energy and Natural Resources Committee

staff, Allen Stayman and Joshua Johnson, as they conduct a series of fact finding meetings on issues relating to local immigration control and the CNMI economy. If you have any questions regarding this testimony please do not hesitate to submit them to me and I will respond as soon as possible.

The Commonwealth of the Northern Mariana Islands is committed to being self-sufficient, self-reliant, and able to provide a high standard of living for its people. Unfortunately, we have encountered a few problems and have not been able to reach and maintain this goal. As the subcommittee members are fully aware, the CNMI is currently in a financial depression and that we have yet to find our way out of this crisis.

It is a necessity that we rely on funding that we receive under Compact Impact from OIA to supplement our local funding for schools, health care clinics, police and fire protection, and other basic government services. The continuation of this funding is vital.

We are also dependent on Covenant funding that we receive to build and/or improve our infrastructure. While I would like to ask for a greater share of these funds, I am aware that we have a back log of unspent funding that we must liquidate first.

There are several areas that I would request special consideration for in the FY 2008 budget.

1. I am bothered about the accountability and audit problems that were highlighted in a recent GAO report: U.S. Insular Areas: Economic, Fiscal, and Financial Accountability Challenges. Although throwing money at a problem doesn't always fix it, if this problem needs more staff training, technical expertise, or general technical assistance, I respectfully request that funding be provided to address these needs.
2. As CNMI Government revenues continue to decline our first priority must be to the general welfare of our residents. Shortages in government funding could easily interfere with our responsibilities for immigration and border control. The CNMI Law Enforcement, Labor and Immigration Initiative is currently funded under The OIA Technical Assistance Program. It is my understanding that annual grants have been declining for the past five years or so. I respectfully request that additional funds be provided to the Technical Assistance Program to strengthen this important initiative.
3. Congressional appropriating committees have always earmarked funding for the Close Up Foundation, Junior Statesmen, and the Pacific Business Center out of the Technical Assistance Program. These are worthy organizations and I request that their earmarks be continued.
4. Congresswoman Bordallo has recently introduced H.R. 1075, the United States Territories Infrastructure Bond Bank Authorization Act. I strongly support this bill, and thank her for her leadership in bringing it to a reality. As I am sure that this structure will have great benefits for the CNMI as well as the other territories, funds need to be identified so that the purchasers of these bonds can be paid. I respectfully request that this subcommittee examine ways to allow Compact Impact funding available as leverage for these bonds.
5. Lastly, Madame Chairwoman, I need to ask for additional funds to repair vital infrastructure at the CNMI's only hospital. The back-up generator and reverse osmosis equipment are in need of replacement. The lives of the patients in the Commonwealth Health Center are dependent on stable power and clean water. It is estimated that \$1 million is needed to replace these systems and upgrade the hospital interfaces.

Thank you for this opportunity to share my thoughts on the Office of Insular Affairs' FY 2008 Budget with you today.

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Mrs. CHRISTENSEN. I would also ask your office, Deputy Assistant Secretary Cohen, if you would supply the information on the 10 criteria in the CIP program and, in addition to that, a report on what has occurred in the years of this program has existed with respect to each of the Territories, what were the criteria they were judged on and their funding levels.

Mrs. CHRISTENSEN. A lot came up during this hearing on issues related to the IRS, and we will be looking at perhaps holding a joint hearing with Ways and Means to look at some of the concerns of the Territories with respect to IRS and I don't have to go into

detail on what those might be for the Virgin Islands. You have heard from Ms. Bordallo on some of her concerns. But I want to thank also the Deputy Assistant Secretary Cohen for coming under such difficult circumstances and being patient and waiting for the Governors to be questioned and taking our questions, and of course I want to thank the Governors for being here and for your testimony and for your responses and your recommendations, and I am also very happy that we have reinstituted this Subcommittee and that you have an opportunity to come to the Congress and for us to have this dialogue on the record and to be able to really focus on some of the unique challenges that the Territories face.

The hearing record will be open for 10 days for any responses to additional questions that the Subcommittee members may have. And if there is no further business before the Subcommittee, the Chairman again thanks the members of the Subcommittee and our witnesses, and the Subcommittee stands adjourned.

[Whereupon, at 12:17 p.m., the Subcommittee was adjourned.]

[Additional material submitted for the record follows:]

[A statement submitted for the record by Mr. Faleomavaega follows:]

**Statement of The Honorable Eni F.H. Faleomavaega,  
a Delegate in Congress from American Samoa**

Madame Chairman:

I commend you for holding this hearing which is both necessary and timely. The 2008 budget request for the Office of Insular Affairs (OIA) is \$403.8 million. Of this, \$27.7 million has been requested for critical infrastructure projects (CIPS).

Historically, at least for the past decade or more, the U.S. Department of the Interior has left American Samoa's CIP funds unmarked in the President's budget. In fact, Congress appropriates (through the Covenant) a fixed amount of about \$10 million per year for American Samoa's CIPs based now on a competitive allocation system. These funds are held by OIA until the American Samoa Government (ASG) makes a request or proposal for funding of a specific project.

Over the years, it is my understanding that the Governors and the Fono are supposed to work together in determining what projects should be undertaken. By way of this process, our local leaders were supposed to be assured of having input in how federal dollars are spent and managed in the Territory.

However, this year, OIA and Governor Togiola have pre-determined that \$3 million should be set aside for fiber optics or "economic development" and this has been done without consultation with the Fono and without my knowledge. As a Member of Congress, it is within my purview to earmark CIP funds prior to ASG receiving those funds. However, as a courtesy to our local leaders, I have never earmarked CIP funds even though I may have disagreed with ASG's priorities. The only exception was a \$2 million set aside for emergency medicines and supplies at LBJ.

While I am not against fiber optics and while I actually introduced the Governor and OIA to the idea, I was led to believe that OIA would loan money to ASG for this purpose and was never informed that money would be taken from our CIPs to fund this proposal. American Samoa's CIP funds are used for health and education and these are and must be our highest priorities and we cannot afford to have \$3 million stripped away to fund fiber optics which ultimately will be a \$20 million or more project.

More importantly, I cannot support a process that cuts out the Fono. Again, as a courtesy to our local government, I have never earmarked, or set aside, ASG's CIP funds, although it is within my purview to do so. As a matter of personal policy, I have left it to the discretion of our local leaders to decide how CIP and operations funds should be spent and this is how I believe the process should remain.

However, if the Department of the Interior, OIA, and Governor Togiola intend to stand by their proposal to take \$3 million from our CIP funds without consultation with the Fono, then I will earmark the remaining money to assure that the Fono is represented and that critically needed projects are funded.

I also want to comment about how OIA has labeled this \$3 million for fiber optics. OIA has stated that this is for purposes of "economic development." I believe if OIA was sincerely interested in economic development in American Samoa it would seriously consider the recommendations made by the American Samoa Economic Development Commission.

In 1997 federal legislation was introduced and enacted in 1999 which established a Secretarial Commission to examine American Samoa's economic condition and make recommendations on how to diversify and expand American Samoa's economy. This was the first time in American Samoa's relationship with the United States that a Secretarial Commission was established.

This Secretarial Commission was established at a cost of \$600,000, supported by Presidents Clinton and George W. Bush, chaired by the former Governor of Hawaii John Waihee, and administered by the U.S. Department of the Interior. Governor Tulafono Togiola of American Samoa served as a commission member. I served as an ex officio member.

In conjunction with the people of American Samoa, the Commission developed an economic plan based on the will of the people. In fact, over 8,000 people were surveyed at the request of the Commission by the American Samoa Community College.

In April 2002, the Secretarial Commission issued its final report to the President of the United States and I would like to ask that the Executive Summary be included for the record. The Chair noted that "while the people of American Samoa are ultimately responsible for implementing the plan, they will need the direct assistance and support of the United States Government, in particular the Department of the Interior to succeed."

To date, the U.S. Department of the Interior has failed to move forward on this plan and I must say our local government officials have also not acted. Despite \$600,000 of American taxpayer dollars having been set aside for this purpose, I am disappointed that OIA has dismissed the findings of the Commission and has instead set about spending additional taxpayer dollars on bringing down university students from the mainland who are completely unfamiliar with our culture to develop our economy with no input from the community or even my office and maybe even without input from our local Governor although he is in a better position to know what he has been privy to or not.

I am also disappointed that the OIA recently spent \$92,000 of taxpayer dollars to fund the writing of a federal bill to replace IRS section 936, the possession tax credit. I would like to ask that a copy of this proposed bill be included as a matter of record as well as other pertinent materials relating to this decision. I would also like to note that the proposed bill failed to include input from our canneries, our Fono, our fishing fleet, my office, and other vested stakeholders.

Given that the House Ways and Means Committee and Senate Committee on Finance have jurisdiction for any and all federal tax policy, I am concerned that DOI entered into murky waters by funding the drafting of legislation. Again, the DOI did not fund a report or a study but instead funded the drafting of a bill. It was my impression that this is not the role of federal agencies.

I also have concerns that in addition to funding the writing of legislation, OIA has now provided ASG with \$150,000 to develop an economic strategy to address the impact of the tuna cannery shutdown. Again, I want to point out that \$600,000 was already set aside and expended for the establishment of the American Samoa Economic Development Commission which developed an economic plan based on the will of the people. OIA has also already published a report in July 2006 entitled, "The Economic and Financial Impact of American Samoa Cannery Shutdown on the Territory's Economy, Employment, Public Sector and the Federal Budget." I ask that this report be placed in the record and also all relevant correspondence relating to OIA's decision to spend another \$150,000 to reinvent the wheel.

I would also like to request oversight over OIA's use of technical assistance grant funds which have paid for the above mentioned activities. According to Assistant Secretary Cohen's testimony, "the only funding that can be considered truly discretionary are OIA salaries and expenses (\$8.2 million) and the Technical Assistance activity (\$16.1 million), which account for \$24.3 million out of the total OIA budget of \$403.8 million in FY 2008."

Since OIA set aside \$150,000 in 2007 to develop an economic strategy for American Samoa, then I believe Congress has a right to know what expert has been identified to develop this strategy. I also believe that if we're paying for a strategy we should get a strategy and there should be oversight to make sure we don't get another bill.

Also, if OIA determines that \$92,000 should be set aside for a study about IRS section 936, then I believe a study is what we should get. Instead, we got a bill

which was slipped to the Senate Finance and Energy Committees. I might also add that the bill went nowhere because that is not the way we do business in Congress. In Congress, we introduce our bills in the light of day.

As a complement to federal efforts to develop and diversify American Samoa's economy, I remain hopeful that ASG will propose and enact local tax reform. I believe the Territorial Tax Exemption Board has served its usefulness and ASG now needs to standardize, by law, corporate tax rates, exemptions, tax holidays, and capitalization requirements so that investors and companies that want to conduct business in the Territory will be treated equally under the law.

On the federal side, I also want to say that the original purpose of the possession tax provisions was to enhance the ability of U.S. firms operating in the possessions to compete with foreign firms and section 936 encouraged our tuna industry to stay in American Samoa. However, we cannot be so naive as to think that by resolving the issue of section 936 that we have resolved American Samoa's dependency on the tuna industry. Nothing could be further from the truth. American Samoa's private sector economy continues to be more than 80% dependent, either directly or indirectly, on the U.S. tuna fishing and processing industries and, even with 30A tax credits in place, we have no guarantee that the tuna canneries will stay in American Samoa.

Our tuna industry faces serious challenges as a result of one free trade agreement after another including the Andean and Thailand Free Trade agreements. Thailand is already the biggest exporter of tuna in the world and even the Andean countries can wipe out American Samoa's entire tuna industry. While we have been successful in making sure tuna is considered highly import sensitive, we must be successful in keeping canned tuna in the longest phase out possible and we must protect our albacore base or all of our efforts will be for naught.

But even if we are successful in these areas, American Samoa cannot control world wage rates. For now, a tuna cannery worker in American Samoa is paid about \$3.60 per hour. In Thailand and the Andean countries, cannery workers are paid 60 cents and less per hour. These are the realities facing American Samoa. And this is why almost ten years ago, Congress established a Secretarial Commission to help American Samoa develop a plan to diversify its economy. With its final report issued in 2002, I believe it is now time for OIA and ASG to take action.

In November, the American people overwhelmingly voted to take our country in a New Direction. As a result, I believe it is our duty to make sure all federal agencies, including OIA, operate in a manner that is transparent and inclusive. In other words, I believe OIA should be obligated to make sure that the Fono has a voice in how federal funds from the Department of the Interior are expended in American Samoa and it is my intention to also bring these matters to the attention of the Subcommittee on Interior Appropriations.

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[NOTE: An explanatory memorandum dated August 2, 2005, submitted for the record by Mr. Faleomavaega has been retained in the Committee's official files.]

[A letter submitted for the record by David B. Cohen, Deputy Assistant Secretary for Insular Affairs, follows:]





United States Department of the Interior  
OFFICE OF INSULAR AFFAIRS  
1849 C Street, NW  
Washington, DC 20240



Deputy Assistant Secretary

MAR 12 2007

Honorable Donna M. Christensen  
Chairwoman, Subcommittee on Insular Affairs  
U.S. House of Representatives  
Committee on Natural Resources  
Washington, DC 20515

Dear Mrs. Christensen:

Enclosed, please find the Covenant Capital Improvement Project (CIP) ratings for fiscal years 2005, 2006, 2007, and 2008 as requested by the Subcommittee on Insular Affairs during the oversight hearing on February 27, 2007.

In preparing the fiscal year 2008 budget request, each territory was rated using an identical set of criteria. These criteria evaluated each government's performance on recent Single Audit Reports, compliance with Federal grant requirements, responsiveness to formal requests of OIA, and the strength of the territory's audit office. Each territory's overall rating is derived from the summation of its performance on the set of criteria.

Should you have any questions or comments, please feel free to contact me.

Sincerely,

David B. Cohen

Attachments

[NOTE: Attachments to Mr. Cohen's letter have been retained in the Committee's official files.]

